NO. 89-454

Supreme Court, U.S.
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In the Supreme Court of the United States

OCTOBER TERM, 1989

AMOCO PRODUCTION COMPANY,
Petitioner,

VERSUS

MANUEL LUJAN, JR., SECRETARY,
DEPARTMENT OF INTERIOR,
BARRY A. WILLIAMSON, DIRECTOR,
MINERALS MANAGEMENT SERVICE, AND
THE DEPARTMENT OF INTERIOR,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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QUESTION PRESENTED

Whether it is unlawful for an agency of the United States to nullify a prior binding commitment by retroactively redefining its power to make such a commitment.

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IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1989

No. 89 -

AMOCO PRODUCTION COMPANY,

Petitioner,

VERSUS

MANUEL LUJAN, JR., SECRETARY,
DEPARTMENT OF INTERIOR,
BARRY A. WILLIAMSON, DIRECTOR
MINERALS MANAGEMENT SERVICE, AND
THE DEPARTMENT OF INTERIOR,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The petitioner, Amoco Production Company ("Amoco"),[1] respectfully prays that a writ of certiorari

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[1] Pursuant to Rule 28.1, petitioner states that its parent corporation is Amoco Company which is in turn a wholly owned subsidiary of Amoco Corp. and that all other subsidiaries and affiliates are wholly owned by Amoco Corp., Amoco Company or Amoco Production Company.

issue to review the judgment and opinion of the United States Court of Appeals for the Fifth Circuit, entered in the above entitled proceeding on July 24, 1989.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Fifth Circuit is reported at 877 F.2d 1243, and is reprinted in Appendix A hereto at p. A-1, *infra*. The unpublished order and memorandum ruling of the United States District Court for the Western District of Louisiana (Walter, J.) are reprinted in Appendices B and C hereto at p. A-23 and p. A-25, *infra* respectively. The decisions of the Interior Board of Land Appeals are reported at 94 IBLA 129 and 85 IBLA 121, and are reprinted in Appendices D and E hereto at p. A-36 and p. A-45, *infra*, respectively.

JURISDICTION

On July 24, 1989, the Fifth Circuit entered its opinion affirming the district court's judgment. No petition for rehearing was sought. The jurisdiction of this Court to review the judgment of the Fifth Circuit is invoked under 28 U.S.C. § 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

43 U.S.C. § 1337 Grant of leases by Secretary

(a) Oil and gas leases; award to highest responsible qualified bidder; method of bidding; Congressional consideration of bidding system; notice; annual report to Congress

(1) The Secretary is authorized to grant to the

highest responsible qualified bidder or bidders by competitive bidding, under regulations promulgated in advance, any oil and gas lease on submerged lands of the outer Continental Shelf which are not covered by leases meeting the requirements of subsection (a) of section 1335 of this title. . . . The bidding shall be by sealed bid and, at the discretion of the Secretary, on the basis of —

(A) cash bonus bid with a royalty at not less than 12-1/2 per centum fixed by the Secretary in amount or value of the production saved, removed, or sold;

(B) variable royalty bid based on a percentum in amount or value of the production saved, removed, or sold . . .

(C) cash bonus bid, or work commitment bid based on a dollar amount for exploration with a fixed cash bonus, and a diminishing or sliding royalty . . . not less than 12-1/2 per centum . . . in amount or value of the production saved, removed, or sold;

. . . .

(F) cash bonus bid with a royalty at no less than 12-1/2 per centum fixed by the Secretary in amount or value of the production saved, removed, or sold . . .

(G) work commitment bid based on a dollar amount for exploration with a fixed cash bonus and a fixed royalty in amount or value of the production saved, removed, or sold . . . .

43 U.S.C. § 1344

(a) Schedule of proposed oil and gas lease sales

. . . .

(4) Leasing activities shall be conducted to assure receipt of fair market value for the lands leased and the rights conveyed by the Federal Government.

43 U.S.C.§ 1334 Administration of leasing

(a) Rules and regulations; amendments; cooperation with State agencies; subject matter and scope of regulations

The Secretary shall administer the provisions of this subchapter relating to the leasing of the outer Continental Shelf, and shall prescribe such rules and regulations as may be necessary to carry out such provisions. The Secretary may at any time prescribe and amend such rules and regulations as he determines to be necessary and proper in order to provide for the prevention of waste and conservation of the natural resources of the outer Continental Shelf, and the protection of correlative rights therein, and, notwithstanding any other provisions herein, such rules and regulations shall, as of their effective date, apply to all operations conducted under a lease issued or maintained under the provisions of this subchapter. . . .

30 C.F.R. § 250.64 (1954)

The value of production, for the purpose of computing royalty, shall be the estimated reasonable value of the product as determined by the supervisor, due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field or area, to the price received by the lessee, to posted prices, and to other relevant matters. Under no circumstances shall the value of production of any of said substances for the purposes of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale of thereof or less than the value computed on such reasonable unit value as shall have been determined

have been determined by the Secretary. In the absence of good reason to the contrary, value computed on the basis of the highest price paid or offered at the time of production in a fair and open market for the major portion of like-quality products produced and sold from the field or area where the leased lands are situated will be considered to be a reasonable value.

30 C.F.R. 250.64 (1979)

The value of production shall never be less than the fair market value. The value used in the computation of royalty shall be determined by the Director. In establishing the value, the Director shall consider: (a) the highest price paid for a part or for a majority of like-quality products produced from the field or area; (b) the price received by the lessee; (c) posted prices; (d) regulated prices; and (e) other relevant matters. Under no circumstances shall the value of production be less than the gross proceeds accruing to the lessee from the disposition of the produced substances or less than the value computed on the reasonable unit value established by the Secretary.

STATEMENT OF THE CASE

Amoco invoked the jurisdiction of the district court under 43 U.S.C. § 1349(b)(1). Amoco also invoked the jurisdiction of the district court under 28 U.S.C. §§ 1331 (federal question) and 1337 (commerce). This case raises a substantial question concerning retroactive application of new agency policy to invalidate pre-existing commitments by the agency. The decision below also is important because of its substantial financial repercussions within the offshore oil industry and its effects on the relationship between the United States and its mineral lessees.

Amoco is a lessee of federal offshore Lease OCS-G 1972, issued by the Department of Interior, covering East Cameron Block 33, Offshore Louisiana. This case arises out of a dispute between Amoco and the Department of Interior over Amoco's obligation to pay royalties on gas produced from that lease. Under Amoco's interpretation of two binding royalty value determination letters issued by the United States Geological Survey ("USGS"),[2] royalties were properly paid. According to a new policy of the Department of Interior, however — a policy which was not articulated until after the royalties in question were paid — the letters, as interpreted by Amoco, violate the applicable statutes and regulations, and therefore do not protect Amoco from retroactive assessment of additional liability. Because the sequence of events is important in understanding Amoco's position, the pertinent events are set out in chronological order.

The first event pertinent to this proceeding occurred on June 29, 1966. On that date, Amoco furnished to the MMS' predecessor, the USGS, copies of the gas purchase contract between Amoco and Florida Gas Transmission Company ("Florida Gas") dated November 20, 1964, (A.R. Tab 37, Exh. H) and the Certificate of Public Convenience and Necessity issued by the Federal Power Commission ("FPC") in docket No. CI 65-584, covering the sales made pursuant to that contract. (A.R. Tab 33, p. 2, *et seq*). This submission was made pursuant to the existing version of

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[2] At the time that the valuation letters were issued, the USGS was the agency of the Department of Interior responsible for valuing, for royalty purposes, oil and gas produced from federal offshore leases. This responsibility was transferred from the USGS to the Minerals Management Service ("MMS") in 1982. 47 Fed. Reg. 4751 (1982). Thus, while the valuation letters involved were issued by the USGS, the order to pay additional royalties which gave rise to this lawsuit was issued by the MMS.

30 C.F.R. § 250.46 (1954) (A.R. Tab 11, Exh. C, p. 1), which allowed but did not require the lessee to submit contracts for approval. Although this contract initially did not cover sales of gas produced from Lease OCS-G 1972, both the submitted contract and the submitted FPC certificate clearly stated that gas would be sold from various other OCS leases to satisfy the requirements of the contract.

The next pertinent event occurred on July 31, 1972, when Amoco and Columbia Gas Transmission Corporation ("Columbia") executed a gas purchase and sales agreement covering fifty percent of the gas underlying Lease OCS-G 1972 and committing fifty percent of the gas underlying the lease to Columbia (the "Columbia contract"). In compliance with the then applicable regulatory provision, Amoco also forwarded copies of the Columbia contract to the USGS.[3]

Soon thereafter, Amoco received a letter from the Oil and Gas Supervisor, Gulf of Mexico Area, USGS, dated August 31, 1972 (the "1972 valuation letter"), in which the USGS acknowledged receipt of the Columbia contract and stated: "Payment on the gas for royalty purposes shall be based on the field delivery volume times the FPC-approved price, or a higher price, if received." (p. A-19, *infra*). Also in 1972, Columbia Gulf Transmission Corporation ("Columbia Gulf") contracted with Amoco to transport the gas to be sold by Amoco to Florida Gas. Columbia Gulf applied for a transportation certificate from the Federal Power Commission ("FPC") in 1972, but that certificate was not issued until 1977.

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[3] The provision applicable at that time required lessees to file "within thirty days after the effective date thereof copies of all contracts for the disposal of lease products." 30 C.F.R. § 250.47 (1969) (A.R. Tab 11, Exh. C, p. 2). Amoco fully complied with this requirement and its predecessor with respect to the contracts at issue.

Meanwhile, in reply to the 1972 valuation letter, Amoco mailed a letter to the Oil and Gas Supervisor, dated February 20, 1973, setting forth Amoco's proposed basis for the payment of royalty on Amoco's share of gas produced from lease OCS-G 1972. That letter specifically informed the USGS that only fifty-percent of Amoco's share of the gas from the lease was being sold to Columbia under the Columbia contract. In acknowledgment, a second royalty valuation letter dated March 9, 1973 (the "1973 valuation letter"), was sent by the Acting Oil and Gas Supervisor in which he noted that Amoco had committed only fifty percent of its share of the gas from Lease OCS-G 1972 to Columbia and further stated: "The gas value shall be the lease delivery volume times the FPC-approved price or a higher price if received . . . ."

The next pertinent event was the FPC's granting of the transportation certificate mentioned above to Columbia Gulf in 1977. Following the granting of that certificate, Amoco began delivering all of its gas produced from Lease OCS-G 1972 to Florida Gas under the Florida Gas contract in an effort to balance gas deliveries in accordance with Paragraph 1.6 of the Columbia contract.[4]

Then, in February 1977, the USGS determined that the certificated sales price contained in the Florida Gas contract, which the MMS and the IBLA would later reject as the basis for royalty valuation in this case, was a proper royalty value for gas produced from three of Amoco's other OCS leases.[5] (A.R. Tab 37, Exh. E). This acceptance of the

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[4] Such balancing was necessitated by the fact that during the previous five-year period, while the transporatation certificate application was pending, Amoco had delivered 100% of its gas from OCS-G 1972 to Columbia as permitted by that contract.

[5] Interestingly, the February 1977, royalty value determination letter was signed by the same individual, Louis E. McBee, who actually signed the 1972 and 1973 royalty valuation letters addressed in this proceeding. The circuit court's reprinting omitted Mr. McBee's signatures.

FPC-approved price was typical of USGS royalty valuations at the time.

For example, in a release dated August 15, 1977, included in the Geological Survey Conservation Division Manual as Part 647, the Department of Interior stated that royalty values for sales of onshore gas subject to FPC jurisdiction:

> . . . from wells commenced prior to June 1, 1977, and which are subject to an arms-length contract entered into prior to that date, . . . shall be established as the higher of:
>
> (1) The price received by lessee or operator in accordance with the provision of the applicable sales contract; or
>
> (2) A minimum value of not less than 18 cents per Mcf at 14.73 psia and 60° F.[6]

The FPC-approved price in question here exceeded the eighteen cent minimum and was the price received under the applicable sales contract. Thus, throughout the period in question, when Amoco paid royalty to the United States based on the Florida Gas contract price, it assumed that it was acting properly in accordance with the policy and practice of the Department of Interior. (A.R. Tab 37, affidavit of Lyle E. Davis).

Nonetheless, on November 17, 1981, the then Under Secretary of the Interior, Donald P. Hodel, initiated,

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[6] *See also* United States Department of Interior, Office of the Solicitor, Memorandum of Law at 16 (Oct. 21, 1977) *reprinted in* 1 Gower Federal Service, *Royalty Valuataion and Management*, GS-151-O&G ("the Department . . . as a matter of policy and practice, generally honors the FPC prices in the case of gas").

through the MMS, a review of Amoco's royalty payments from all OCS leases for gas being sold to Florida Gas to determine whether Amoco was properly valuing such gas for royalty purposes. (A.R. Tab 37, Exh. J). This proceeding culminated in a decision by the Acting Director, MMS, on March 22, 1982, (MMS 82-1) that in effect ordered Amoco to pay the royalty on gas being sold to Florida Gas at a value greatly in excess of the FPC-approved contract price. Amoco appealed this Director's decision to the IBLA. Then, following extensive briefing by both parties, the MMS, by motion dated December 9, 1982, moved for the remand of the case to the Director "due to a reconsideration by MMS of policy issues which represent the gravamen of these cases." (A.R. Tab 21, Exh.1). The following day, on December 10, 1982, the IBLA signed an order remanding the case to the MMS and dismissing Amoco's appeal; and, on the same date, the Acting Director of the MMS addressed a letter to Amoco's counsel notifying Amoco that the MMS' order in MMS 82-1 was vacated and the case dismissed. (A.R. Tab 21, Exh's 2 and 3).

Meanwhile, on September 20, 1982, the Royalty Compliance Office ("RCO") initiated an administrative proceeding by issuing an order to Amoco to pay $1,457,047.00 in additional royalties from Lease OCS-G 1972 for the period September 1977 through October 1981. (A.R. Tab 42). The RCO based this decision on a finding that Amoco had failed to submit to the USGS a transportation agreement and the Florida Gas sales contract in alleged violation of 30 C.F.R. § 250.47. As noted above, the Florida Gas contract had in fact been filed in accordance with the applicable regulation.

Amoco promptly filed an appeal of the RCO order, and on May 17, 1984, the Director, MMS, denied Amoco's appeal and affirmed the RCO order. (A.R. Tab 27, Exh. A).

The Director conceded that the contract price at which Florida Gas bought the gas from Amoco was the "FPC-approved price" and agreed that the Florida Gas contract was submitted by Amoco to the USGS, but concluded that the value determination letters, which established the value of gas being produced as the "FPC-approved price," were only "intended" to refer to the FPC-approved price under the contract with Columbia.

Following an appeal of this decision, the IBLA, on February 15, 1985, issued its decision in *Amoco Production Co.*, 85 IBLA 121 (1985) (hereinafter occasionally referred to as "Amoco I") (p. A-45, *infra*). In affirming the Director's decision, the IBLA rejected the Director's interpretation of the "intent" of the value determination letters and found instead that Amoco had complied with the terms of those letters in paying royalties based upon the "FPC-approved price" under the Florida Gas contract. In concluding that royalty was due, the IBLA found that the royalty valuations were *superseded* by and contrary to Department of Interior regulations then found at 30 C.F.R. § 250.64. 85 IBLA at 129 (p. A-58, *infra*).

Recognizing the troublesome legal ramifications of the IBLA's analysis, the MMS soon filed a motion for clarification or reconsideration. In that motion the MMS sought clarification of:

(1) the relationship among: (a) a royalty valuation set forth in a value determination letter; (b) the requirement in 30 C.F.R. 210.150 to submit sale contracts for each lease; and (c) the regulations governing royalty value contained in 30 C.F.R. 206.150; and

(2) the agency's discretion to collect royalties at less than the "highest price received for similar gas."

(A.R. Tab 13). In its subsequently filed memorandum in support, the MMS expanded its list of items to be clarified and, alternatively, requested that the February 15, 1985, decision be reconsidered "to determine whether the decision in this case has overruled *sub silentio* the Board's frequently cited decision in *Superior Oil Co.*" (A.R. Tab 11 at 14). Among other things, *Superior Oil Co.* stands for the proposition that royalty valuation letters are binding on the government and on the lessee to which they are issued. *See* 12 IBLA at 223 (R.116). Amoco supported the MMS' motion to the extent that it sought reconsideration of the IBLA's holding that the MMS' value determination letters were superseded by and contrary to 30 C.F.R. § 250.64, but opposed the remainder of the MMS' motion.

On October 9, 1986, the IBLA issued its decision in *Amoco Production Co. (On Reconsideration)*, 94 IBLA 129 (1986) (p. A-36, *infra*) (hereinafter occasionally referred to as "*Amoco II*"), "clarifying" its earlier decision and modifying that decision by deleting certain parts. Disregarding its previous findings of fact and with no factual additions to the record, the IBLA reversed its earlier conclusion regarding Amoco's compliance with the valuation letters by determining that "there was no *intent* on the part of MMS to be bound by the terms of that [Florida Gas] contract with respect to the production from OCS-G-1972." 94 IBLA at 132 (A-42, *infra*) (emphasis added). The IBLA further determined that such an interpretation would have been an unlawful delegation to the lessee of the Director's discretionary authority to establish royalty values. Consequently, the IBLA held that all of the gas produced from the lease was to be valued based upon the price established in the Columbia contract. The legal basis for the IBLA's conclusion had been drastically revised, but the outcome remained unchanged.

The district court, in a memorandum ruling entered October 3, 1988, (Appendix C, A-23, *infra*), upheld the IBLA's determination on the grounds that a "rational basis existed for the IBLA determinations," and that "[a]s a rational basis for the decision existed, clear error is not present." The Fifth Circuit affirmed the district court, although it recognized that the valuation procedure was retroactive and "not . . . ideal." The Fifth Circuit's affirmance depended on its finding that the IBLA acted within its authority in finally concluding, on reconsideration, that applicable statutes and regulations reasonably could be interpreted by the IBLA to prohibit the USGS from "delegating" its authority to value gas, as was ostensibly required according to the IBLA under Amoco's construction of the letters. The circuit court's acceptance of the reasonableness of this conclusion allowed that court to uphold the IBLA's decision and to permit the Director to establish a new royalty value retroactively.

REASON FOR GRANTING THE WRIT

The shifting, inconsistent and result-oriented approach of the Department of Interior raises an important and far reaching question of potential significance not only to offshore lesses, but to all who contract with the government: May the United States retroactively invalidate unfavorable binding commitments to its citizens through belated determinations that those unfavorable commitments were, in retrospect, *ultra vires*?[7] The decisions

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[7] Contrary to the characterization made below by counsel for the Secretary, Amoco is not arguing here that the government should be estopped. This is not a case in which an agent or officer of the government authorized a private party to act in a clearly prohibited manner. Were that the case, Amoco might fall subject to the general rule that "the Government may not be estopped on the same terms as any other litigant." *Heckler v. Community Health Services of Crawford County,*

below indicate an alarming willingness to condone such retroactive invalidation. This condonation establishes a new and disturbing precedent which stands in stark contrast against the position of other courts and agencies in similar cases. Because of the significance of this precedent, this case has importance far beyond the particular facts and parties involved, and therefore warrants the Court's attention.

Footnote 7 continued.
Inc., 467 U.S. 51, 60 (1984). *But see United States v. Lazy FC Ranch*, 481 F.2d 985, 989-90 (9th Cir. 1973) (where a government official has caused individuals to take action that was not clearly prohibited at the time it was taken, the government would be estopped).

The law of estoppel seems irrelevant because this case turns on whether a private citizen is entitled to rely on a binding commitment by an agency despite a subsequent new interpretation of the agency's powers which renders such commitments invalid. The government's authority cited below, *Atlantic Richfield Co. v. Hickel*, 432 F.2d 587 (10th Cir. 1970), does not address this issue. *See Phillips Petroleum Co. v. Dept. of Energy*, 449 F. Supp. 760, 794-95 and n.157 (D. Del.), *aff'd, Standard Oil Co. v. Dept. of Energy*, 596 F.2d 1029 (Temp. Emer. Ct. App. 1978) (*Atlantic Richfield's* pronouncements concerning estoppel were "completely inapposite" where issue was binding nature of auditors' prior advice that had been rendered in a manner consistent with the contemporaneous regulatory scheme). Although the Department's avoidance of its lawful commitments does not appear to involve customary estoppel analysis, it has the same potential to create "considerable ferment" and to generate inconsistent treatment throughout the courts of appeals. *See Schweicker v. Hansen*, 450 U.S. 785, 791 (1981) (Marshall, J., dissenting).

This question also touches on what Professor Davis considers "*one of the major anomalies of the present legal system* . . . [that] an agency may not make new law by adjudication and apply the new law both retroactively and prospectively, without providing procedural protection through . . . notice and comments." 4 Davis, *Administrative Law Treatise* § 20:8 at 30 (1983) (emphasis in original). While resolution of the present case does not require the court to directly address that anomaly, Professor Davis' observation highlights the possibility that decisions in this area will be inconsistent.

It is undisputed that the commitment in question is of the sort that ordinarily binds the Department of Interior.[8] The particular binding obligation at issue is the Department's duty to accept as a proper value for royalty purposes for gas sold from Lease OCS-G 1972, "the FPC-approved price, or a higher price if received." It is undisputed that Amoco always has paid royalty based on "the FPC-approved price" found in the pertinent contracts, and that Amoco did not receive a price higher than "the FPC-approved price." Moreover, the Department does not dispute that the 1972 and 1973 valuation letters, by their terms, approved both the Florida Gas and Columbia "FPC-approved" prices.[9]

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[8] As explained above, both the MMS and Amoco jointly petitioned the IBLA for a rehearing after the IBLA, in its first decision, found that valuation letters of the sort issued to Amoco were not binding on the lessee and the government. *See supra* at 11-12; *see also Amoco Production Co. (On Reconsideration)*, 94 IBLA 129 at 130 (p. A-37, *infra*); *Superior Oil Co.*, 12 IBLA 212, 232 (1973) (R. 116).

[9] In their brief to the Fifth Circuit the respondents stated:

> Amoco incorrectly assumes that the Board rejected Amoco's use of the Florida Gas contract price for royalty valuation purposes because the Board read the term "FPC-approved" in the royalty valuation letters as referring only to the Columbia Gas contract price. *The IBLA decision on reconsideration contains no such determination, but rather affirms the Board's prior determination of the scope of the letters* in *Amoco I*, 85 IBLA at 127. 94 IBLA at 133.

Brief for Appellees at 31-32 (emphasis added).

Even if there were an ambiguity in the valuation letters which brought the use of the Florida Gas price into question, any such ambiguity would be construed in Amoco's favor, under the time-honored rule of interpretation *contra proferentem* ("against the profferer"). *See Restatement (Second) of Contracts*, § 206 (2d ed. 1981). As explained by the IBLA in

What the Department of Interior improperly claims, however, is that because the Florida Gas FPC-approved contract price was not specifically designated by Amoco as being applicable to production from the lease, it is unlawful to construe the 1972 and 1973 valuation letters to include the FPC-approved price under that contract. Allegedly, such construction unlawfully "would result in a delegation to a lessee of the discretionary authority to set the value of gas sold." 94 IBLA at 131 (p. A. 40, *infra*). the Department also improperly found that Amoco was bound to use the Columbia price as royalty value for one-half of the gas sold at all times, regardless of the "FPC-approved price" at which the gas was actually sold.[10]

Footnote 9 continued.
a very similar case involving USGS valuation letters, where there are two possible and reasonable meanings of such a document, "a court, employing the doctrine of *contra proferentem* will adopt that one which is less favorable in its legal effect to the party who chose the words." *Superior Oil Co.*, 12 IBLA 212, 224 (1973)(R. 117) (applying doctrine of *contra proferentem* against the Supervisor, USGS, when interpreting valuation letters written by the Supervisor). Thus, the government, as author of the valuation letters would not be entitled to benefit from an ambiguity here.

[10] This error was affirmed in the circuit court's opinion on the incorrect ground that Amoco never challenged this conclusion:

> *Amoco concedes that* under the letters it was committed to sell half of its gas under the Columbia Gas contract, and that *for royalty purposes it had to value half of its gas at the Columbia Gas contract price, even if none of the gas were sold to Columbia Gas.* Amoco would apparently like to have the benefit of the accounting adjustment denied by the Board, but *at no point in its appeal of the Board's decision has Amoco made any argument specifically directed at the Board's conclusion that the adjustment is impermissible for royalty valuation purposes.*

The Department of Interior's conclusion that the letters were invalid *ab initio* depends entirely on the Department's retroactive application of a new interpretation of the pertinent statutes and regulations. Nothing on the face of those statutes and regulations prohibits the Secretary from declaring that, under a particular lease, FPC-approved prices would be accepted as proper royalty values, and nowhere is there an express statutory or regulatory requirement that valuation be done on a contract-by-contract basis. Thus, the "unlawful delega-

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Footnote 10 continued.
877 F.2d at 1240, (p. A-15, *infra*)(emphasis added). In fact, throughout these proceedings, Amoco had contested the conclusion that the Board could automatically value one-half of the gas sold under the Florida Gas contract at the Columbia price. In its last brief filed with the Circuit court, Amoco noted:

> The Secretary's argument that only 50% of the amount is now disputed, raised in footnote 17 of his brief, is wishful thinking. He suggests that Amoco is barred from challenging the government's assessment of royalty on 50% of the gas sold during the period in question, because Amoco has not challenged the IBLA's "determination that the company's 'accounting adjustment', which reflected its actual sales, was *not* applicable to the value of production for royalty purposes." In fact, *Amoco has challenged the entire assessment, on the grounds that no further royalty is owed because royalty based on the "FPC-approved price" was paid in full.* The Secretary's strained attempt to remove half the amount in question from dispute is nonsensical. *See generally* Amoco's Initial Brief at 10, 26-27 (discussing gas balancing agreement, and showing that all gas, during the period in question, was sold to Florida Gas Transmission Company ("FGT") at the "FPC-approved price").

Reply Brief for Appellant at 2, n.1 (emphasis added).

tion" rule relied on by the IBLA is an agency creation, arising from the Department's interpretation of statues and regulations.

This new agency creation runs counter to the past policy and practice of the Department of Interior which, both at the time the valuation letters were issued and during the period when Amoco paid the royalties now in dispute, indicated that the type of valuation letter now in issue was perfectly proper and was not an unlawful delegation.[11] Not only did the USGS routinely establish "the FPC-approved price, or a higher price if received," as the measure of royalty value under offshore leases, but it specifically approved the FPC-approved price under the identical Florida Gas contract as a proper royalty value for several other offshore leases. Thus, had Amoco resubmitted the Florida Gas contract at the time sales began under that contract (which it was not required to do), the Florida Gas "FPC-approved" price probably would have been accepted as a matter of routine. As late as 1981, the Department of Interior had not formulated the interpretation used by the IBLA here, and the Department in fact admitted that it was unable to formulate a position which would require Amoco to pay the royalties now sought.

As shown by the subsequent decisions of the IBLA in *Amoco I* and *Amoco II*, a similar but unconfessed in-

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[11] As set out above, the USGS' own written interpretation of its royalty valuation duties, where arm's-length sales of gas from wells subject to FPC jurisdiction commenced prior to June 1, 1977, were involved, was that "the base value for royalty purposes" would routinely "be established as the higher of: (1) the price received by the lessee or operator in accordance with the provisions of the applicable sale contract; or (2) a minimum value of not less than 18 cents per Mcf." Conservation Division Manual, Part 647 at 6. Nowhere did the Department intimate that it would consider letters approving royalty value as "the FPC-approved price" to be unlawful delegations of authority.

ability to formulate a clear position persisted until much later. Certainly, at the time that the royalties in dispute were paid, the Department of Interior had neither intimated nor articulated the interpretation now being applied. Instead, the only policy of the Department of which Amoco was aware was that the Department would accept FPC-approved prices as proper royalty value, without any consideration of whether such acceptance constituted some sort of impermissible delegation of Secretarial authority.

And, such acceptance of FPC-approved prices seemed perfectly reasonable in light of the Department of Interior's duty to analyze carefully and to attempt to minimize potential conflicts between its royalty policies and the gas pricing policies of the FPC. *See generally Burlington Truck Lines, Inc. v. United States,* 371 U.S. 156, 173 (1962); *Local 1976, United Brotherhood of Carpenters and Joiners v. NLRB,* 357 U.S. 93, 111 (1958). Thus, the circuit court is incorrect to suggest that the burden was on Amoco to protect against later retroactive invalidation by clarifying the precise meaning and scope of the valuation letters.

Furthermore, it is inconsistent with fundamental principles of administrative law for the IBLA's new determination of departmental policy to be applied retroactively. Generally, new rules and policies of administrative agencies may be applied retroactively only where such retroactive application would not unfairly prejudice those subject to the new rule or policy. *See generally Linkletter v. Walker,* 381 U.S. 618, 628 (1965); 4 K. Davis, *Administrative Law Treatise,* § 20:7 (1983). The Department of Interior itself acknowledges the validity of this rule by its longstanding policy against giving retroactive effect to a subsequent, different interpretation of a statute, where such effect would be prejudicial to private parties' rights

and interests.[13]

Nor is it consistent with principles of government contracts law for the Department to invalidate retroactively the valuation letters in question. Such principles are directly applicable under the IBLA's decision in *Superior Oil Co.*, which states that a valuation letter is "an element in the contract" between the government and the lessee. 12 IBLA at 223 (R. 116). Under well-established contract law principles, where the United States has assumed a contractual obligation, that obligation cannot be avoided retroactively on the basis that it is inconsistent with subsequently developed rules or policies of the contracting agency. *Lockheed Aircraft Corp. v. United States*, 192 Ct. Cl. 36, 426 F.2d 322 (1970); *Bray v. United States*, 43 Ct. Cl. 315 (1908). Moreover, even if there were some inchoate or unarticulated agency rules or policies in existence at the time of contracting, such unformed or secret rules or policies cannot be used to invalidate the government's contractual

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[13] *See Safarik v. Udall*, 304 F.2d 944, 949 (D.C. Cir.), *cert. denied sub nom., Hansen v. Udall*, 371 U.S. 90 (1962). Similarly, the principles underlying Amoco's petition are recognized in the Internal Revenue Service's procedure regarding the effect to be given to erroneous technical advice that has been issued to taxpayers in continuous transactions. The pertinent portion of the applicable Revenue Procedure states:

> However, *if a ruling is issued covering a continuing action or a series of actions and it is determined that the ruling was in error,* or no longer in accord with the position of the Service, *the Associate Chief Counsel* (Technical and International) *ordinarily will limit the retroactivity of the revocation or modification to a date that is not earlier than that on which the ruling is modified or revoked.* To illustrate, if a taxpayer receives a ruling that certain payments are excludable from gross income for federal income tax purposes and it is later determined that the ruling is in error or no longer in accord with the position of the service, the Associate Chief Counsel (Technical and International)

obligations.[14]

The general principle underlying Amoco's position was aptly stated by Mr. Justice Brown, nearly a century ago:

> It is especially objectionable that a construction of a statute favorable to the individual citizen should be changed in such manner as to become retroactive, and to require from him the repayment of moneys to which he had supposed himself entitled, and upon the expectation of which he had made his contracts with the government.

United States v. Alabama G. S. R. Co., 142 U. S. 615, 621 (1892).[15] If contracts with the government are to have meaning, it is important that this principle be protected against the sort of unlawful encroachment condoned by the circuit court.

Footnote 13 continued.

> ordinarily will restrict the retroactive application of the revocation or modification of the ruling.

Rev. Proc. 88-1, *reprinted in* 1989 9 Stand. Fed. Tax Rep. (CCH) ¶ 6005.16 at 67,229 (emphasis added). This statement by the Internal Revenue Service recognizes that where a continuing series of actions (such as the periodic royalty payments here) is involved, an error in the Service's initial advice to the taxpayer or a change in policy will not retroactively invalidate the initial advice, but will revoke the ruling only as of the date of modification or revocation.

14 *See, e.g., NI Industries, Inc. v. United States*, 841 F.2d 1104, 1107-08 (Fed. Cir. 1988); *Turney v. United States*, 126 Ct. Cl. 202, 115 F. Supp. 457 (1953) (contract for sale of surplus property which included radar equipment was not voidable by the government on the ground that an undisclosed directive prohibited disposal of radar equipment); *Electrospace Corp.*, ASBCA 14520, 72-1 B.C.A. (CCH) ¶ 9455 at 43,926 (1972) ("An internal instruction does not have the effect of a statute or regulation published in the Federal Register and is not binding on appellant absent his knowledge of its existence.").

15 Nor would it be permissible for the Department of Interior to reinterpret retroactively the meaning of the letters themselves, as opposed to

CONCLUSION

The general issue raised in this petition is whether the government may invalidate its commitments retroactively by redefining its power to bind itself. The more precise issue is whether the terms of contractually binding royalty valuation letters issued to Amoco by the United States Geological Survey in 1972 and 1973 should be given effect. Under the plain language of these letters, Amoco was entitled to pay royalties on gas produced from the lease in question by multiplying the "field delivery volume times the FPC-approved price, or a higher price, if received."

The Department of Interior, unsatisfied with the amount of Amoco's royalty payments, ultimately has decided that the letters should not be taken at face value. Instead, according to a new interpretation of its statutory and regulatory authority articulated by the Department in the midst of these proceedings, the letters are to be considered invalid to the extent they approve any price other than the specific FPC-approved price found in the particular contract that was submitted at the time Amoco first sold gas from the lease.

Footnote 15 continued.

[14] the meaning of the Department's regulations. In a case similar to the one at bar, several ranchers and other interested individuals ("permittees") filed suit against the Department of Interior and the Bureau of Indian Affairs ("BIA") challenging the administrative agency's interpretation of grazing permits. *Danks v. Fields*, 696 F.2d 572 (8th Cir. 1982). The Department of Interior, through the BIA, administered the grazing permit program and established the rental rate charged to permit holders. Although the permits contained a deadline for the reevaluation of grazing fees, the BIA Area Director increased the amount charged two months after the deadline had passed. While administrative appeals were pending, the permittees requested the district court to issue a preliminary injunction against the fee increase. The district court granted Interior's motion for summary judgment and affirmed the Director's decision. On appeal, the permittees argued, *inter alia*, that the

By condoning the Department's retroactive invalidation of its obligation to accept "the FPC-approved price," the courts below established an unfortunate precedent that conflicts with decisions of other courts and government agencies. Because of the far reaching implications of this undesirable precedent, it is important that this Court review the circuit court's decision and prevent the Department of Interior from assessing royalties in a manner inconsistent with the valuation letters. By so doing, the Court also will discourage other agencies of the United States from retroactively redetermining their authority so as to escape their binding commitments.

For these reasons, and because the decision of the circuit court is incorrect, Amoco Production Company respectfully requests that its Petition for Writ of Certiorari to the Fifth Circuit be granted.

Respectfully submitted,

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Footnote 15 continued.
fee increase was invalid under the terms of the permit issued by the Department of Interior. The Eighth Circuit agreed, and overturned the district court on the ground that the BIA could not alter the terms of the permits through post-issuance interpretations.

APPENDIX A

AMOCO PRODUCTION CO.,
Plaintiff-Appellant

v.

Manuel LUJAN, Jr., Secretary of the
Department of Interior, et al.,
Defendants-Appellees.

No. 88—4797.

United States Court of Appeals,
Fifth Circuit.

July 24, 1989.

Appeal from the United States District Court for the

Western District of Louisiana.

Before JOLLY, HIGGINBOTHAM, and SMITH, Circuit Judges.

PATRICK E. HIGGINBOTHAM, Circuit Judge:

The Director of the Minerals Management Service ordered Amoco to pay certain royalties upon gas produced by Amoco from land leased to it by the United States. The Interior Board of Land Appeals affirmed the Director's order. Amoco appealed the Board's decision in federal district court, contending that the Board had misinterpreted the regulations governing valuation of gas for royalty purposes, and had also misinterpreted valuation letters issued by the government. Amoco contended that the Secretary of the Interior Department was bound by the valuation letters, and that the Board had erroneously permitted the Secretary to value Amoco's production at a rate higher than that specified in the letters. Amoco also raised constitutional arguments, contending that the Secretary's efforts to escape the effect of the letters violated the Due Process Clause. On cross-motions for summary judgment, the district court rejected Amoco's arguments. Amoco now takes a further appeal to this court.

We find that the Board acted within its authority by concluding that federal regulations prohibited the federal officers charged with responsibility for valuing gas from delegating the authority to do so, and by further concluding that the construction of the letters contended for by Amoco would involve such a delegation. We therefore affirm the Board's conclusion that the Director retained discretion to value the disputed portion of Amoco's gas deliveries. We further find that the Director's valuation of the gas was a reasonable exercise of his discretion. We

reject Amoco's argument that the Department's action in this case runs afoul of constitutional restrictions. The judgment of the district court is affirmed.

I

A. The Factual Core

The Interior Department leases land to Amoco. When Amoco sells gas, the Department is entitled to royalties. The parties dispute how much is owed by Amoco to the Interior Department as a result of some sales by Amoco to Florida Gas Transmission Co.

The royalties due on Interior Department leases are computed in part on the basis of "valuation letters" issued by the Department to the lessee. The Department sent valuation letters to Amoco in connection with the lease in 1972 and 1973, when Amoco entered into a contract to sell gas from the lease to Columbia Gas Transmission Company. The question before us is whether those letters bound the parties to a particular royalty valuation with respect to the later sales to Florida Gas, and, if so, what that price was.

B. Regulatory Scheme

The Outer Continental Shelf Lands Act of 1953 (OCSLA), as amended, 43 U.S.C. §§ 1331 *et seq.*, authorizes the Secretary of the Interior to grant leases to private individuals or companies for the recovery of minerals, including oil and gas, from the subsoil and seabed of the

Outer Continental Shelf. 43 U.S.C. § 1337. Under the Act, the Secretary is required to "assure receipt of fair market value for the lands leased and the rights conveyed by the Federal Government." 43 U.S.C. § 1344(a)(4). The Act authorizes the Secretary to require that lessees pay the government a percentage royalty "in the amount or value of the production saved, removed, or sold." 43 U.S.C. § 1337(a)(1)(A).

The Secretary is also authorized by the Act to "prescribe such rules and regulations as may be necessary and proper to carry out" the Act's provisions. 43 U.S.C. § 1334(a). Pursuant to this authority, the Secretary has issued regulations which establish the applicable standard for determining "the value of production" for royalty valuation purposes. In 1954, the Secretary issued 30 C.F.R. 250.64, a regulation directing the Supervisor of the United States Geologic Survey to determine production value for royalty valuation purposes:

> The value of production, for the purpose of computing royalty, shall be the estimated reasonable value of the product as determined by the supervisor, due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field or area, to the price received by the lessee, to posted prices, and to other relevant matters. Under no circumstances shall the value of production of any of said substances be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof or less than the value computed on such reasonable unit value as shall have been determined by the Secretary. In the absence of good reason to the contrary, value computed on the basis of the highest price paid or offered at the time of production in a fair and open market for

the major portion of like-quality products produced and sold from the field or area where the leased lands are situated will be considered to be a reasonable value.

30 C.F.R. 250.64 (1954-79).

The rule was unchanged until 1979, when it was amended to state explicitly that "the value of production shall never be less than the fair market value." 30 C.F.R. 250.64 (effective Dec. 13, 1979). The new rule sipulated [sic] that "the computation of royalty shall be determined by the Director" of the Minerals Management Service, and instructed the Director to "consider" certain factors "[i]n establishing the value";

> The value of production shall never be less than the fair market value. The value used in the computation of royalty shall be determined by the Director. In establishing the value, the Director shall consider: (a) the highest price paid for a part or for a majority of like-quality products produced from the field or area; (b) the price received by the lessee; (c) posted prices; (d) regulated prices; and (e) other relevant matters. Under no circumstances shall the value of production be less than the gross proceeds accruing to the lessee from the disposition of the produced substances or less than the value computed on the reasonable unit value established by the Secretary.

30 C.F.R. 250.64 (1979). In 1983 the rule was redesignated as 30 C.F.R. 206.150, and has since been amended again. Neither party contends that the subsequent amendment matters to the disposition of this lawsuit.

Both applicable versions of the regulation establish the gross proceeds obtained by the lessee as a floor for the

royalty value of the gas produced, but posit a range of reasonable values from which the Director determines the "value of production" for royalty purposes in a specific case. The royalty value may properly be the minimum value, or may be above the minimum, based on consideration of the several listed factors, including the prices paid in other sales of like-quality products from the field or area.

Lessees are required by 30 C.F.R. 210.150 (formerly designated first as 30 C.F.R. 250.46, and later amended and redesignated in 1969 as 30 C.F.R. 250.47), to "file with the Director, within 30 days after their effective date, a copy of all contracts, including all contract modifications (e.g., amendments and terminations), for the disposal of lease products." Lessees submit royalty payments on a monthly basis, 30 C.F.R. 218.50, subject to a later audit by the Royalty Compliance Office, 30 C.F.R. 217.200. The audit, which concerns the amount of royalties submitted, is informed in part by the monthly production and sales reports sent to MMS by the lessee, as well as royalty valuation letters which the Director may have issued with regard to particular contracts for the disposal of lease products.

C. Factual Details

Amoco is a joint tenant of an Outer Continental Shelf lease from the Interior Department, called Lease OCS-G 1972. The lease was created in 1970 and did not originally involve Amoco, but Amoco succeeded to the interest of one of the lessees sometime before August 1972. Amoco has a half-interest in the lease, and must pay royalties accordingly.

In August 1972, Amoco submitted to the United States Geologic Survey (which the parties call, "USGS") a

contract between Amoco and Columbia Gas for the sale of gas from the lease. The Geologic Survey returned a letter indicating that "payment on the gas for royalty purposes shall be based on the field delivery volume times the FPC-approved price, or a higher price, if received." The Geologic Survey sent another letter, pertaining to the same contract with Columbia Gas and containing similar language about royalties, in 1973. Until 1977, Amoco sold exclusively to Columbia Gas, and paid royalties based upon the price which the Federal Power Commission ("FPC," later succeeded by 'FERC," the Federal Energy Regulatory Commission) had approved for those sales. The 1972 and 1973 letters are reprinted as appendices A and B of this opinion.

The import of the valuation letters is complicated further because Amoco's 1972 submission indicated that the Columbia Gas contract would cover only 50% of Amoco's production from the lease. The Geologic Survey's 1973 letter makes clear that the Department understood as much. However, Amoco had problems selling the remaining 50% because of difficulty closing a transportation contract with Columbia Gulf Gas Transmission Company. Amoco sorted matters out with Columbia Gulf in 1977, and then stopped selling to Columbia Gas, apparently in order to balance the 1972-77 deliveries with 1977-82 non-deliveries for the purpose of bringing total Columbia Gas deliveries down to the promised 50% of production.

The meaning and effect of these valuation letters is the heart of the dispute between Amoco and the Secretary. Amoco contends that the Survey's letters valued Amoco's gas production according to the FPC-approved price at which the gas was actually sold, regardless of to whom the gas was sold, so long as at least 50% of Amoco's total reserves from the lease were sold to Columbia Gas under the contract referenced in the letters. The Secretary con-

tends that the letters' reference to "FPC-approved price" is a reference limited to the price approved for the Columbia Gas contract, or, alternatively, that the letters are void insofar as they authorize the valuation of gas at the FPC-approved price for an unspecified contract. This disagreement is important because Amoco eventually sold gas from the lease to Florida Gas Transmission at an FPC-approved price below the FPC-approved price for the Columbia Gas contract.

In 1977 Amoco began selling gas from the lease exclusively to Florida Gas Transmission. The Florida Gas sales were based on a 1964 contract between Amoco and Florida Gas. The 1964 contract had been submitted upon its creation to the Geologic Survey, but at that time Amoco did not know where the gas would come from. Of course, Amoco could not have predicted that the gas would come from the lease in question here, since that lease—much less Amoco's interest in it—did not exist at the time that Amoco submitted the Florida Gas contract.

There was an "FPC-approved price" for the gas sold by Amoco to Florida Gas. That price was lower than the FPC-approved price applicable to the Columbia Gas contract. Between 1977 and 1982, Amoco paid royalties based upon the FPC-approved price for the Florida Gas contract.

The Mineral Management Service Royalty Compliance Office audited Amoco at some point. The Compliance Office concluded that Amoco should have been paying royalties based upon the price approved for the Columbia Gas contract, not the Florida Gas contract. The RCO reasoned that the valuation letters sent in 1972—the only letters ever sent to Amoco in connection with the sale of gas from the land during the time period in question—referred to the "FPC-approved price" for the Columbia Gas

contract, and not to the "FPC-approved price" for any contract pursuant to which Amoco made sales from the lease. The Compliance Office in 1982 demanded 1.458 million dollars from Amoco. Amoco contested the demand.

D. The Proceedings

Amoco appealed the Director's decision to the Department's Interior Board of Land Appeals. The Board heard the case twice, and issued rulings sufficiently confusing that their meaning is a central question dividing the parties. In its first opinion, the Board relied on the 1979 amendment to 30 C.F.R. 250.64, which, according to the Board, preempted the otherwise binding effect of the valuation letters. On this ground, the Board upheld the Director's assessment of a deficiency.

Neither side agreed with this argument, and both sought rehearing. After consideration, the Board retracted its earlier argument, and put forward a new one. The parties contest the *ratio* of that decision. The Board's second opinion is reprinted as Appendix C to this opinion. Our interpretation of the Board's opinion is set out in Part III, below.

Amoco appealed the Board's determination to the federal district court for the Western District of Louisiana. The district court summarized the findings of the Board, and affirmed on the ground that the findings had a "rational basis" and so did not show "clear error." Amoco took an appeal to this court.

II

[1] Neither party questions our jurisdiction. We pause, however, to distinguish this case from *Amoco Pro-*

duction Co. v. Hodel, 815 F.2d 352 (5th Cir.1987), *cert. denied*, — U.S. —, 108 S.Ct. 2898, 101 L.Ed.2d 932 (1988), a very similar case involving the same parties. In that case, this Court dismissed the suit on the ground that it was a claim for money damages against the government cognizable only in the Claims Court. In the earlier case, however, Amoco had paid the demanded royalties, whereas here Amoco has refused to pay and has instead posted a bond. This difference is crucial, 815 F.2d at 361 n. 10 (jurisdiction turns on whether Amoco owes the fees, or instead seeks restitution of fees paid), and the district court so found. The government, which apparently pressed the jurisdictional issue in the earlier case, agrees. We find no jurisdictional defect in this case.

III

[2,3] Our review of the district court's decision granting summary judgment is *de novo*. On review of an agency adjudication, however, the reviewing court must in general affirm the decision unless the agency's action was "arbitrary, capricious, or otherwise not in accordance with law." 5 U.S.C. § 706(2)(A); *see also Camp v. Pitts*, 411 U.S. 138, 142-43, 93 S.Ct. 1241, 1244, 36 L.Ed.2d 106 (1973). We must honor the agency's interpretation of the law authorizing agency action so long as the interpretation is a reasonable one. *Chevron U.S.A. Inc. v. Natural Resources Defense*, 467 U.S. 837, 104 S.Ct. 2778, 2781-82, 81 L.Ed.2d 694 (1984). The parties dispute the application of these standards to review of agency decisions interpreting written contracts. Amoco contends that the interpretation of a contract may be reviewed *de novo*. Even without resolving this argument, we find it clear that our review of administrative issues depends upon the exercise of appropriate deference to the agency. We must therefore begin our inquiry by identifying the exact basis for the agency's

action, including the extent to which the agency purports to interpret a written contract.

The interpretation of the Interior Board of Land Appeals' decision in this case is unusually difficult, and is a bone of contention between the parties. The Secretary appears to have relied upon three different theories--through the Director's original demand for royalties, and then the two Board opinions—in order to collect the royalties disputed by Amoco. Amoco contends that the Secretary's ultimate rationale in the second Board opinion, like the original rationale underlying the Director's post-audit charge, turns upon interpretation of the valuation letters. The Secretary contends that the rationale turns upon interpretation of the regulations governing the Department's valuation authority. In order to facilitate discussion of the issue, we have reprinted the two valuation letters and the second Board decision as appendices to this opinion.

We are largely in agreement with the Department's interpretation of the second Board opinion. The Board divided the royalty computation into two periods: the initial 5-year period (1972-77) when all the gas went to Columbia Gas, and the second period (1977-81) when all the gas went to Florida Gas. The Board's argument respecting both periods hinges on the fact that Amoco submitted to the Survey a contract for the sale of half of its gas to Columbia Gas, and that the Survery's valuation letters assumed that half of the gas would be sold to Columbia Gas. No contract governing the remaining portion of the gas was submitted to the Survey at any time after Amoco acquired its interest in the lease.

The gist of the Board's ruling is that during each period, the valuation letters governed the royalty value of

all gas produced by Amoco from the lease. However, during each period, 50% of the gas sold by Amoco was committed to Columbia Gas, and so had to be valued for royalty purposes at the FPC-approved price for the Columbia Gas contract. While the letters purported to value the remaining gas according to the FPC-approved price applicable to whatever contract it might be sold under, that valuation was, the Board held, void as an unauthorized delegation of the Director's responsibility to value gas on a case-by-case basis. The Director consequently retained discretion to value the gas pursuant to the regulations. The Board concluded that there was no abuse of discretion.

The Board arrived at this interpretation of the letters by the following reasoning. The Board first observed that during the initial period, 50 percent of the gas sold by Amoco was covered by the Columbia Gas agreement. The remaining 50 percent of Amoco's share during that first period was also sold to Columbia Gas. The royalties for this "remaining gas" were to be determined on the basis of "the value of equivalent gas as established by the Columbia Gas agreement." 94 IBLA 129, 130 (1986) (citing 30 C.F.R. 218.50). Amoco wished to assign some of the Columbia Gas sales to later years, and conversely assign later Florida Gas sales to the earlier years, but the Board concluded that "the value of production (for royalty purposes) is not subject to the accounting adjustment proposed by Amoco." *Id.*

The Board then confronted the more difficult second period, when all of Amoco's gas was sold to Florida Gas. The Board first reaffirmed its conclusion, announced in its original disposition of Amoco's arguments, that "[T]he valuation of the gas produced under lease OCS-G 1972 is governed by the August 1972 and March 1973 Survey value determination letters. Neither letter had been

challenged or amended and they remained applicable for royalty determinations for gas produced during that time period." *Amoco Production Co.*, 94 IBLA at 131, *quoting Amoco Production Co.*, 85 IBLA 121, 127 (1985). The context of the quoted passage from the Board's earlier opinion makes clear that the Board was finding that all of Amoco's production share, rather than merely the 50 percent attributable to the Columbia Gas contract, was governed by the valuation letters.

The Board went on to hold that because the valuation letters from 1972 and 1973 had never been rescinded, Amoco was bound to pay royalties on 50% of the gas produced from the lease as though the gas had been sold to Columbia Gas under the submitted contract. "[V]aluation of gas produced from lease OCS-G-1972 was governed by the value determination letters. We specifically find this to be the case for the 50 percent of Amoco's production committed to Columbia Gas. The Columbia Gas contract submitted by Amoco committed 50 percent of the production from OCS-G 1972 to Columbia Gas, and, for that portion of the production, the 1972 and 1973 letters were binding on MMS *and the producer,* unless and until rescinded and modified." 94 IBLA at 132 (emphasis in the original) (citing 30 C.F.R. 250.47). The Board refers to gas that is "committed," rather than gas that is "sold;" the Board is here referring to the period when *none* of Amoco's gas was in fact sold to Columbia Gas.

On this theory, because the contract committed Amoco to sell 50% of its production from the lease to Columbia Gas during the second as well as the initial period, and because the Board refused to permit the accounting adjustment whereby Amoco would assign sales from the initial period to the second period, 50% of the gas sold during the second (1977-82) period was to be valued according to

the Columbia Gas contract.

This line of reasoning leaves only the second half of Amoco's gas sold during the second period unaccounted for. The Board then found that "for the 50 percent of the gas not committed to Columbia Gas, the royalty determination by MMS was clearly within the discretionary authority of the Secretary as set forth in 30 C.F.R. 250.64." 94 IBLA at 133. This conclusion relied on the Board's nondelegation doctrine, developed earlier in the Board's opinion. Because 30 C.F.R. 250.64, both before and after amendment, required the Director (before amendment, the Supervisor) to make case-specific assessments of the royalty value of gas sold under particular contracts, the Director had no authority to delegate the valuation function to Amoco, or any other party, by valuing the gas according to any unspecified contract that Amoco might select. The valuation letters were for that reason void insofar as they purported to value half of Amoco's gas at the FPC-approved price for an as yet undetermined contract. Because the Survey's letters to Amoco could not delegate discretion to decide valuation of the gas, and because the second half of the gas sold to Florida Gas was not covered by the contract, the Director retained authority to set the valuation pursuant to 30 C.F.R. 250.64. The Board concluded its reasoning by finding that the Director did not abuse his discretion by valuing the gas sold to Florida Gas at the FPC-approved price for the Columbia Gas Contract.

IV

Once the Board's rationale is made clear, the complexity of this case largely dissolves. Amoco devotes much of its brief to argument about the meaning of the valuation letters. Yet the Board appears for the most part to have accepted Amoco's interpretation of the letters. The Board

agrees with Amoco that the letters valued all of Amoco's production from the lease at the FPC-approved price of the contract under which the gas was actually sold. Amoco concedes that under the letters it was committed to sell half of its gas under the Columbia Gas contract, and that for royalty purposes it had to value half of its gas at the Columbia Gas contract price, even if none of the gas were sold to Columbia Gas. Amoco would apparently like to have the benefit of the accounting adjustment denied by the Board, but at no point in its appeal of the Board's decision has Amoco made any argument specifically directed at the Board's conclusion that the adjustment is impermissible for royalty valuation purposes.

After accounting for the apparent agreement between Amoco and the Board about the meaning of the letters, and likewise accounting for the aspect of the Board's interpretation not challenged by Amoco's appeal, the remaining controversy narrows considerably. At issue is only the valuation for royalty purposes of the second, "uncommitted" half of Amoco's sales to Florida Gas during the second of the two periods identified by the Board. But as our description of the Board's opinion should make clear, the Board's treatment of this portion of the gas depends not on a contested interpretation of the valuation letters, but rather on an interpretation of the agency's regulations that vitiates the effect of the letters. The Board's valuation of the "uncommitted" gas sold to Florida Gas accepts, rather than rejects, Amoco's interpretation of the letters. Despite the great ingenuity of Amoco's arguments, its efforts to characterize this suit as a contracts case fail.

[4] Amoco is therefore bound by conventional administrative law standards of review, regardless of what we might think of Amoco's theories about the relation between contract law and administrative law. Amoco can

defeat the Secretary's application of the Department's regulations to this case only by showing that application to be "arbitrary, capicious, or otherwise contrary to law." Judged by this standard, Amoco's arguments are unsuccessful. The Board's conclusions clearly derive from the text of 30 C.F.R. 250.64, which requires the "supervisor" to determine the value of production. The pre-amendment (up until Oct. 26, 1979) regulation said, "The value of production, for the purpose of computing royalty, shall be the estimated reasonable value of the product *as determined by the supervisor.*" The post-amendment regulation says, "The value used in the computation of royalty shall be determined by the Director." There is nothing arbitrary or capricious about reading this language to impose a non-delegable duty upon the Department to fix royalty valuation on a contract-by-contract basis.

It might still be possible to contend that the Board's construction of the regulation is nonetheless arbitrary and capricious because it permits the Department to benefit from its own misleading language—that is, by purporting to delegate its authority, the Department effectively "sets Amoco up" for a later decision retroactively establishing an unfavorable rate. However, a lessee which *presumes* a delegation, and fails to cover itself by submitting the contracts it intends to use to modify the valuation scheme, cannot claim to be the victim of double-dealing by the department. Lessees are under an obligation to "file with the supervisor within 30 days after the effective date thereof copies of all contracts for the disposal of lease products." 30 C.F.R. 250.47 (1969, since renumbered). Had Amoco re-filed the Florida Gas contract with the Survey before beginning to use that contract as the basis for its royalty payments, and had the Survey issued no valuation letter to supplement the letters issued in connection with the Columbia Gas contract, whether the Department could

reasonably construe its regulations to give itself a "second shot" at setting the valuation rates might well give us pause.

This case differs, however, because Amoco did not resubmit the Florida Gas contract before beginning its sales to Florida Gas from lease 1972. Amoco points out that the Florida Gas contract had been submitted to the Survey in 1964, when executed, but the contract did not, and could not, then refer to the lease (which was not created until 1970). Without a subsequent notice to the Survey, tying the contract to the lease, there is no reason to believe that the Survey has indicated to Amoco that the Florida Gas contract may be used as a basis for the royalty computation. As the Board indicated in its opinion on rehearing, "While a copy of the Florida Gas contract had been submitted to MMS, there is ample evidence that there was no intent on the part of MMS to be bound by the terms of that contract with respect to the production from OCS-G-1972." 94 IBLA at 132.

It is true, as Amoco takes pains to point out, that the Florida Gas contract had been submitted to the Survey in 1964, and that 30 C.F.R. 250.47 did not appear to require resubmission of the contract. But the question we are now considering is *not* whether Amoco complied with 30 C.F.R. 250.47. Rather, the question is whether Amoco's submission of the Florida Gas contract renders "arbitrary and capricious" the Board's interpretation of 30 C.F.R. 250.64. And the answer to that question *does* depend upon when the Florida Gas contract was submitted.

V

[5] Finally, Amoco contends that the Board's ruling violates the Fifth Amendment, either because it is a con-

fiscatory taking or because it "shocks our sense of fair play" and so deprives Amoco of substantive due process. Amoco relies heavily on two cases which are in fact predicated upon Texas law, not the federal Constitution. *See Flowers v. Diamond Shamrock Corp.*, 693 F.2d 1146, 1154 (5th Cir.1982), and *Bowers v. Phillips Petroleum Co.*, 692 F.2d 1015, 1017 (5th Cir.1982) (both following *Exxon Corp. v. Middleton*, 613 S.W.2d 240 (Tex.1981)).

The only other case cited by Amoco in connection with its constitutional argument is *Boutte v. Chevron Oil Co.*, 316 F.Supp. 524 (E.D.La.1970). *aff'd*, 442 F.2d 1337 (5th Cir.1971), which is also inapplicable. *Boutte* was a procedural due process case pertaining to wheteher a particular royalty obligation became due prior to an FPC determination affecting the total proceeds from a sale, or whether the royalties on the contested portion of the proceeds became due only after the determination. By contrast, Amoco's argument here sounds not in procedural due process but in substantive due process. Amoco's constitutional argument thus has no support in precedent.

VI

We can understand Amoco's objection to a valuation procedure that has the appearance of being both retroactive and unfavorable. Although we lack a detailed familiarity with royalty practices in connection with offshore leasing, the events that precipitated this suit do not seem ideal. But we do not sit in review of agency action to determine what is ideal or best for the agency to do. The mandate of the federal courts is a narrower one, that of checking agency action which is "arbitrary and capricious, or otherwise not in accordance with law." Amoco's counsel has labored assiduously to show that the Department's action fails to conform even to this rather deferential stand-

ard. We are, however, unpersuaded.

For the reasons given, the judgment of the district court is in all respects

AFFIRMED.

APPENDIX A

GEOLOGIC SURVEY'S LETTER OF 8/31/72 TO AMOCO

Gentlemen:

We have received your Gas Purchase and Sales Agreement dated July 31, 1972, *with Columbia Gas Transmission Corporation, covering the sale of your share of the gas produced from lease** OCS-G 1972, East Cameron Block 33. In the future, it is necessary to send only one copy of these contracts.

Payment on the gas for royalty purposes shall be based on the field delivery volume times the *FPC-approved price,** or a higher price, if received.

In the event that this gas is processed, we shall require a copy of the processing agreement. Before processing begins, you will need to apply for an approved method of royalty payment for the processed liquids under 30 CFR 250.67.

---

* Italics in the circuit court's appendix reflect handwritten underlining on the copy of the exhibit that was submitted to the circuit court. No such emphasis appeared in the original letter to Amoco.

Pursuant to 30 CFR 250.47, please forward a copy of the FPC certificate for the sale of this gas.

Sincerely,

Robert F. Evans
Oil and Gas Supervisor
Gulf of Mexico Area

cc:

Contracts File:

Buyer—Columbia Gas

Seller—Amoco (w/atch)

Lease OCS-G 1972

Accounting

FLBoyd:seh

APPENDIX B

GEOLOGIC SURVEY'S LETTER OF 3/9/73 TO AMOCO

Gentlemen:

Amoco owns 50% of lease OCS-G 1972, East Cameron Block 33, and Mobil has the remaining 50%. Amoco has committed 50% of its share of the gas from this lease to Columbia Gas, with the remaining 50% of its share being uncommited

at this time.

Processing of your above-committed gas will be accomplished in Amoco's South Pecan Lake Plant. The raw make from this plant is fractionated in Cities Service's Lake Charles Fractionation Plant. Cities Service charges Amoco fees for this fractionation as specified in your Hydrocarbon Fractionation Agreement, a copy of which you enclosed with your letter of February 20, 1973.

Effective with the initiation of processing at Amoco's South Pecan Lake Plant, the gas and plant liquids value for royalty purposes, pursuant to 30 CFR 250.67, for Amoco's share of the gas from the above lease shall be determined as the total of:

1. The plant product liquids value shall have a *base* factor of 45%. A certain fractionation and transportation charge shall be allowed as follows:

a. *For ethane:* The resulting value shall be 45% of the recovery volume times the price after fractionation minus $0.42 per gallon.

b. *For propane:* The resulting value shall be 45% of the recovery volume times the price after fractionation minus $0.52 per gallon.

c. *For butanes and heavier:* The resulting value shall be 39.825% (100.0% minus 11.5% times 45%) of the recovery volume times the price after fractionation, provided the price is reasonable and in line with industry standards.

2. The gas value shall be the lease delivery volume times the FPC-approved price or a higher price if received, minus

3. The value, computed at the same price, of Plant Volume Reduction gas.

For royalty purposes, the total value shall not be less than the lease delivery volume times the FPC-approved price or a higher price if received.

Pursuant to 30 CFR 250.47, please send us a copy of the FPC certificate for the sale of this gas.

Sincerely yours,

D.W. Solanas
Acting Oil and Gas Supervisor
Gulf of Mexico Area

APPENDIX C to the Fifth Circuit's opinion, which reprinted the text of the IBLA's decision in *Amoco Production Co.* (*On Reconsideration*), 94 IBLA 129 (1986), is omitted, as it has been included as Appendix D to this Petition.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF LOUISIANA MONROE DIVISION

FILED
OCT 12 1988

AMOCO PRODUCTION CO.

versus

CIVIL ACTION NO. 87-0243
JUDGE WALTER

DONALD P. HODEL, SECRETARY OF THE DEPARTMENT OF THE INTERIOR, ET AL.

O R D E R

Pursuant to the Memorandum Ruling dated October 3, 1988, the last paragraph beginning on page five and continuing on page 6 should read as follows:

> "Initially, the jurisdiction issue must be examined. This Court has jurisdiction over this matter pursuant to Section 23(b)(1) of the Outer Continental Shelf Lands Act, 43 U.S.C. § 1349(b) (1), and under 28 U.S.C. §§ 1331(a) and 1337. The case of *Amoco Production Co. v. Hodel*, 815 F.2d 352 (5th Cir. 1987), does *not* preclude this Court's jurisdiction in this matter. In *Amoco Production Co.*, Amoco sought review of the Secretary's decision in another royalty dispute in which Amoco had paid the disputed amount *prior* to seeking administrative and judicial review of the order to pay the additional royalties. The Fifth Circuit characterized Amoco's suit as a suit for money

damages cognizable only in the United States Claims Court under the Tucker Act, 28 U.S.C. §§ 1346(a)(2) and 1491(a). *Id.* at 361 n. 10. Because Amoco in the case at bar has not paid the disputed amount to the government, but has posted a bond in lieu of payment, the decision in *Amoco Production Co.*, is inapplicable."

THUS DONE AND SIGNED at Monroe, Louisiana, this 12 day of October, 1988.

/s/ Donald E. Walter

DONALD E. WALTER
UNITED STATES DISTRICT JUDGE

APPENDIX C

IN THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF LOUISIANA

MONROE DIVISION

FILED
OCT 3 1988

AMOCO PRODUCTION CO.

versus

CIVIL ACTION NO. 87-0243
JUDGE WALTER

DONALD P. HODEL, SECRETARY OF THE DEPARTMENT OF THE INTERIOR, ET AL.

MEMORANDUM RULING

Plaintiff, Amoco Production Company ("Amoco"), brought this action for declaratory judgment and injunctive relief seeking review of two decisions by the Secretary of the Interior ("Secretary"), through the Interior Board of Land Appeals ("IBLA"), issued in *Amoco Production Co.*, 85 IBLA 121 on February 15, 1985, and 94 IBLA 129 on October 9, 1986. Plaintiff has exhausted all administrative remedies. Cross-motions for summary judgment have been filed by the plaintiff and the defendants pursuant to Federal Rule of Civil Procedure 56(a) and 56(b).

The dispute in this case concerns the valuation for royalty purposes of gas sold to Florida Gas Transmission Company ("FGT") by Amoco from Lease OCS-G 1972, East Cameron Block 33, Offshore Louisiana, in which Amoco is the owner of a one-half interest. Mobil Oil Cor-

poration ("Mobil") and the Pan American Petroleum Corporation ("Pan American") entered into Lease OCS-G 1972 with the United States through the Secretary in September, 1970. Amoco later purchased Pan American's interest in this lease. The United States receives royalties, in cash or in kind, from this production. The time period of the valuation in question spans from September, 1977 through October, 1981.

Inititally, in 1964, Amoco and FGT entered into a warranty contract for the sale of natural gas. Subsequent to the making of this contract, Amoco furnished the United States Geological Society ("USGS") copies of the gas purchase contract and the Certificate of Public Convenience and Necessity issued by the Federal Power Commission ("FPC"). This certificate set the FPC-approved price for the gas sales contract. Although this contract did not initially cover sales of gas produced from Lease OCS-G 1972, both the contract and the FPC certificate stated that gas would be sold from various other Outer Continental Shelf leases to satisfy the requirements of the contract.

Later, in July, 1972, Amoco and Columbia Gas Transmission Company ("Columbia") executed a Gas Purchase and Sales Agreement covering a portion (50 percent) of Amoco's production from Lease OCS-G 1972. Amoco forwarded to the USGS copies of this contract. No additional copies of the FGT contract indicating that production from Lease OCS-G 1972 would be used to meet this warranty contract were furnished to the USGS at this time. The valuation for payment of royalties for the natural gas for the Columbia contract was based on the field delivery volume times the FPC-approved price, or a higher price if received.

Also in 1972, Amoco contracted with Columbia Gulf

Transmission Corporation ("Columbia Gulf") to transport the gas to be sold by Amoco to FGT from Lease OCS-G 1972 production. Due to delays in obtaining a transportation certificate, initially one hundred percent of Amoco's gas was delivered to Columbia under the contractual balancing provision contained in the Columbia contract. During this period, Amoco paid royalties based upon the FPC-approved price for the sale to Columbia.

Following the FPC's issuance of a transportation certificate to Columbia Gulf in 1977, Amoco commenced delivery of one hundred percent of the gas produced from Lease OCS-G 1972 to FGT in an effort to balance gas deliveries as authorized under the Columbia contract. During this time period (September 1977 to October 1981), Amoco paid royalties based upon the FPC-approved price for the sale to FGT.

In 1981, the Department of the Interior ("DOI") reviewed all OCS leases from which Amoco was selling gas to FGT. This proceeding culminated in a decision by the Acting Director of the Minerals Management Service ("MMS") on March 22, 1982, ordering Amoco to pay royalties on the gas being sold to FGT at the value received under the Columbia contract price. Amoco appealed this decision to the IBLA. The case, however, was remanded to the MMS on December 9, 1982, upon a motion for remand filed by the Director. Amoco was notified the following day that the MMS order was vacated and the case dismissed.

On September 20, 1982, the Royalty Compliance Office ("RCO") initiated this administrative proceeding by issuing an order to Amoco to pay $1,457,847.00 in additional royalties from Lease OCS-G 1972 for the period September, 1977 through October, 1981. Amoco appealed this order. On May 17, 1984, the Director denied Amoco's appeal and

affirmed the RCO order.

Following an appeal of the Director's decision, the Interior Board of Land Appeals ("IBLA") on February 15, 1985, issued its decision in *Amoco Production Co.*, 85 IBLA 121 (1985), affirming the Director's decision. Under this ruling, the IBLA noted that Amoco had complied with earlier value determination letters concerning royalty payments under the FGT contract by paying the FPC-approved price; however, it determined that the royalty valuations were superceded by and contrary to the DOI regulation at 30 C.F.R. § 250.64 (redesignated and presently contained at 30 C.F.R. § 206.150). Shortly thereafter, the MMS filed a motion for Clarification or Reconsideration *En Banc* of the IBLA's February 15, 1985, decision. The IBLA determined that MMS did not intend to be bound by the terms of the FGT contract with respect to the production from OCS-G 1972. All gas produced from this lease was to be valued based upon the price established in the Columbia contract.

OPINION

In filing its action for declaratory judgment and injunctive relief, Amoco contends that:

> (1) Jurisdiction of this Court over this controversy exists under Section 23(b)(1) of the Outer Continental Shelf Lands Act, 43 U.S.C. § 1349(b)(1), and under 28 U.S.C. §§ 1331(a) and 1337; and
>
> (2) Both the February 15, 1985, and October 9, 1986, decisions constitute final action by the Secretary through the IBLA, and consequently, both should be reviewed; and

(3) The decision by the Secretary as pronounced by the IBLA is unlawful as it is arbitrary, capricious and has the effect of establishing a royalty in excess of the value imposed by the FPC.

On the other hand, the defendants urge the following claims:

(1) Jurisdiction may not be proper in this Court due to the decision of the Fifth Circuit in *Amoco Production Co. v. Hodel*, 815 F.2d 352 (5th Cir. 1987), *cert. denied*, 56 U.S.L.W. 3894 (June 28, 1988) (No. 87-372);

(2) Only the October 9,1986, decision by the IBLA constitutes a final decision by the Secretary; and

(3) The plaintiff has not carried its burden of proof in showing that the IBLA's final decision is "clearly erroneous."

Initially, the jurisdiction issued must be examined. This Court has jurisdiction over this matter pursuant to Section 23(b)(1) of the Outer Continental Shelf Lands Act, 43 U.S.C. § 1349(b)(1), and under 28 U.S.C. §§ 1331(a) and 1337. The case of *Amoco Production Co. v. Hodel*, 815 F.2d 352 (5th Cir. 1987), does preclude this Court's jurisdiction in this matter. In *Amoco Production Co.*, Amoco sought review of the Secretary's decision in another royalty dispute in which Amoco had paid the disputed amount *prior* to seeking administrative and judicial review of the order to pay the additional royalties. The Fifth Circuit characterized Amoco's suit as a suit for money damages cognizable only in the United States Claims Court under the Tucker Act, 28 U.S.C. §§ 1346(a)(2) and 1491(a). *Id.* at 361 n. 10. Because Amoco in the case at bar has not paid

the disputed amount to the government, but has posted a bond in lieu of payment, the decision in *Amoco Production Co.*, is inapplicable.

Next, the issue of the finality of the two IBLA decisions concerning this controversy should be covered. As noted earlier, the first decision, *Amoco Production Co.*, 85 IBLA 121, decided February 15, 1985, was reconsidered in *Amoco Production Co.*, 94 IBLA 129, and decided on October 9, 1986. This Court finds that the decision upon rehearing constitutes final agency action. This determination is consistent with the general notion that an administrative agency's order or decision is not final for the purposes of judicial review until outstanding petitions for reconsideration have been disposed of. *Nordell v. Heckler*, 749 F.2d 47, 48 (1984), *citing Civil Aeronautics Board v. Delta Air Lines*, 367 U.S. 316, 326, 81 S.Ct. 1611, 1619, 6 L.Ed.2d 869, 877 (1961).

Finally, the third issue is whether the IBLA committed "clear error" upon reconsideration of this controversy. Under the Administrative Procedure Act ("APA"), 5 U.S.C. § 706, the reviewing court may hold unlawful and set aside agency actions, findings, and conclusions found to be "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." The ultimate standard of review is a narrow one. *Citizens to Preserve Overton Park v. Volpe*, 401 U.S. 402, 416, 91 S.Ct. 814, 824, 28 L.Ed.2d 136, 153 (1970). This Court is limited to review of the administrative record. *See Camp. v. Pitts*, 411 U.S. 138, 142, 93 S.Ct. 1241, 1243-44, 36 L.Ed.2d 106, 11 (1973).

Most importantly, a reviewing court should not replace a governmental agency's judgment with its own, unless a rational basis for the agency's judgment does not exist. *Bowman Transportation, Inc. v. Arkansas-Best*

Freight System, 419 U.S. 281, 290, 95 S.Ct. 438, 444, 42 L.Ed.2d 447, 458 (1974); *Ethyl Corp. v. EPA*, 541 F.2d 1, 34 (D.C. Cir. 1976), *cert. denied*, 426 U.S. 941, 96 S.Ct. 2662, 49 L.Ed.2d 394 (1976). Clear error must exist in order to overturn an agency's decision. *Overton Park*, 401 U.S. at 416, 91 S.Ct. at 824, 28 L.Ed.2d at 153. It is well established that the Secretary of the Interior has the authority and considerable discretion to establish royalty values of production from federal oil and gas leases. *United States v. Ohio Oil Co.*, 163 F.2d 633 (10th Cir. 1947); *Continental Oil Co. v. United States*, 184 F.2d 802 (9th Cir. 1950); *Marathon Oil Co. v. United States*, 604 F.Supp. 1375 (D. Alaska 1985), *aff'd* 807 F.2d 759 (9th Cir. 1986), *cert. denied*, ___ U.S. ___, 107 S.Ct. 1593, 94 L.Ed.2d 782 (1987); *Amoco Production Co.*, 29 IBLA 234 (1977).

When deciding this controversy upon reconsideration, the IBLA analyzed various pieces of legislation, including two versions of 30 C.F.R. § 250.64[1] The August 31,

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[1] The version of 30 C.F.R. § 250.64 applicable from September 1977, to October 26, 1979, read as follows: "The value of production, for the purpose of computing royalty, shall be the estimated reasonable value of the product as determined by the supervisor, due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field or area, to the price received by the lessee, to posted prices, and to other relevant matters. Under no circumstances shall the value of production of any of said substances for the purposes of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof or less than the value computed on such reasonable unit value as shall have been determined by the Secretary. In the absence of good reason to the contrary, value computed on the basis of the highest price paid or offered at the time of production in a fair and open market for the major portion of like-quality products produced and sold from the field or area where the leased lands are situated will be considered to be a reasonable value." As of October 26, 1979, the regulation was amended to read as follows: "The value of production shall never be less than the fair market value. The value used in the computation of royalty shall be determined by the Director. In establishing the value, the Director shall consider: (a) The

1972, and March 9, 1973, survey royalty value determination letters from the Oil and Gas Supervisor, Gulf of Mexico Area, USGS, to Amoco concerning the Columbia contract and Lease OCS-G 1972 were reviewed.[2]

After careful consideration of all legislation and correspondence between the parties, this Court finds that a rational basis existed for the IBLA determinations that:

> (1) valuation of 50% of Amoco's production which was committed to Columbia Gas was governed by the August 31, 1972, and March 9, 1973, valuation letters, pursuant to 30 C.F.R. § 250.47 (1982); hence, the IBLA correctly found that the FPC-approved price for the Columbia contract governed the royalty valuation for this gas;
>
> (2) the other 50% of Amoco's production not com-

Footnote 1 Continued.
highest price paid for a part or for a majority of like-qualty products produced from the field or area; (b) the price received by the lessee; (c) posted prices; (d) regulated prices; and (e) other relevant matters. Under no circumstances shall the value of production be less than the gross proceeds accruing to the lessee from the disposition of the produced substances or less than the value computed on the reasonable unit value established by the Secretary."

[2] On August 23, 1972, Amoco forwarded the USGS copies of the Columbia contract. Amoco later received a letter from the Oil and Gas Supervisor, Gulf of Mexico Area, USGS, dated August 31, 1972, in which the USGS acknowledged receipt of the Columbia contract and stated that "[p]ayment on the gas for royalty purposes shall be based on the field delivery volume times the FPC-approved price, or a higher price, if received." Later, by letter dated March 9, 1973, the Acting Oil and Gas Supervisor acknowledged that Amoco had only committed 50% of its share of the gas from Lease OCS-G 1972 to Columbia and established the basis for the for [sic] payment of the royalties for both natural gas liquids and natural gas. With regard to natural gas, the Supervisor stated that "[t]he gas value shall [sic] the lease delivery volume times the FPC-approved price or a higher price if received. . . ."

mitted under the Columbia Gas contract was properly valued under 30 C.F.R. § 250.64. As noted earlier, this provision allowed for royalty determination based upon a price for the product of the well which had been accepted by the parties as being either the "estimated reasonable value" (pre-1979) or "fair market value" (post-1979) of the gas. The FPC-approved price under the Columbia Gas contract met both the pre-1979 and post-1979 criteria. It was the only value that had been placed on gas under the lease. Consequently, its use in the valuation of the royalty under the Florida Gas contract was proper.

(3) Amoco could not claim that the Florida Gas contract price was binding based upon the conclusion that it was an FPC-approved price which could be substituted for the Columbia Gas FPC-approved price under the value determination letters of August 31, 1972, and March 9, 1973. Furthermore, the rejection of Amoco's argument that no higher price had been received under the Florida Gas contract (hence, this price would prevail for gas sold to Florida Gas) was also rational. Allowing such a substitution by Amoco would result in the delegation to the lessee of the discretionary authority to set the value of the uncommitted gas sold. This would be contrary to the provisions of 30 C.F.R. § 250.64.

As a rational basis for this decision existed, clear error is not present. The decision upon reconsideration of the IBLA is AFFIRMED and the defendants' cross-motion for summary judgment is GRANTED.

THUS DONE AND SIGNED at Monroe, Louisiana, this 30th day of September, 1988.

/s/ Donald E Walter

DONALD E. WALTER
UNITED STATES DISTRICT
JUDGE

COPY SENT:

DATE 10-4-88

APPENDIX C (cont.)

IN THE UNITED STATES DISTRICT COURT FOR
THE WESTERN DISTRICT OF LOUISIANA
MONROE DIVISION

FILED
OCT 3 1988

AMOCO PRODUCTION CO.

versus CIVIL ACTION NO. 87-0243

DONALD P. HODEL, SECRETARY
OF THE DEPARTMENT OF THE
INTERIOR, ET AL.

J U D G M E N T

Pursuant to the foregoing Memorandum Ruling,

IT IS ORDERED that the decision upon reconsideration of the Interior Board of Land Appeals is AFFIRMED; and

IT IS FURTHER ORDERED that defendants' cross-motion for summary judgment is GRANTED.

THUS DONE AND SIGNED at Monroe, Louisiana, this 30th day of September, 1988.

/s/ Donald E. Walter
DONALD E. WALTER
UNITED STATES DISTRICT JUDGE

Judgment Entered 10-4-88

APPENDIX D

UNITED STATES DEPARTMENT OF THE INTERIOR

OFFICE OF HEARINGS AND APPEALS
INTERIOR BOARD OF LAND APPEALS
4015 WILSON BOULEVARD
ARLINGTON, VIRGINIA 22203

AMOCO PRODUCTION CO.
(ON RECONSIDERATION)

IBLA 84-789 Decided October 9, 1986

Reconsideration of *Amoco Production Co.*, 85 IBLA 121 (1985), upon motions submitted by the Minerals Management Service and Amoco Production Company. MMS 82-0046-OCS.

Affirmed as modified.

1. Oil and Gas Leases: Royalties—Outer Continental Shelf Lands Act: Oil and Gas Leases

   The Minerals Management Service (MMS) is authorized to issue royalty value determination letters, which will be binding on the Department and the lessee unless and until resinded or modified by MMS. A royalty value determination letter properly issued by MMS cannot be interpreted in a manner which would result in the delegation of authority for determination of royalty amounts to a lessee. Such a letter must establish the basis for determination in sufficiently specific language to permit the exact basis for determination, and cannot bind the Department to a royalty rate merely because that rate has been approved by the Federal Power Commission.

APPEARANCES: Charles R. Shockey, Esq., Office of the Solicitor, U.S. Department of the Interior, Washington, D.C., for the Minerals Management Service; George J. Domas, Esq., Debora [sic] Bahn Price, Esq., and Bruce V. Schene, [sic] Esq., New Orleans, Louisiana, for Amoco Production Company.

OPINION BY ADMINISTRATIVE JUDGE MULLEN

This is a reconsideration of this Board's opinion in *Amoco Production Co.*, 85 IBLA 121 (1985). In that case Amoco Production Company (Amoco) had appealed from a decision of the Director, Minerals Management Service (MMS), dated May 17, 1984, affirming an order issued by the Chief, Royalty Compliance Office, MMS, Tulsa, Oklahoma, dated September 20, 1982 (revised October 5, 1982), requiring payment of $1,435,852.97 in additional royalties for natural gas produced under lease OCS-G 1972, East Cameron Block 33, Offshore Louisiana, during the period from September 1977 to October 1981. The facts of the case, which have been set forth in detail in *Amoco Production Co., supra*, are not in dispute.

MMS and Amoco Production Company (Amoco) have filed petitions for reconsideration. By order dated May 31, 1985, the Board agreed to reconsider its prior decision and ordered briefing. Both petitioners seek clarification of four points set forth in *Amoco Production Co., supra*. These points are: (1) Do the value determination letters dated August 31, 1972, and March 1973 establish the proper value basis under the regulations for computing Amoco's royalty for its share of production from Outer Continental Shelf oil and gas lease OCS-G-1972? (2) Were the value determination letters superseded by 30 CFR 250.64 (1982)? (3) Were the value determination letters contrary to 30 CFR 250.64 (1982)? (4) To what extent, if any,

does 30 CFR 250.64 (1982), restrict the MMS discretionary power to set a binding royalty value? This opinion will discuss the first two issues at some length. Because of our holding on the first two questions, we do not deem it necessary to address the arguments presented by the parties with respect to the second two.

The fact that the Florida Gas contract was submitted to the Geological Survey on June 29, 1966, is not in dispute. There is also no dispute that, when submitted, it was not the intent of the parties that the Florida Gas contract would be applied to gas produced from OCS-G-1972. In July 1972 Amoco submitted the Columbia Gas contract to MMS for royalty calculation purposes. This contract, which committed 50 percent of the gas produced from OCS-G-1972 to Columbia Gas, was designated as the proper value basis for royalty determinations in the August 31, 1972, value determination letter.

Part of the problem in the analysis of the facts on appeal arises from the fact that Amoco owned 50 percent of the production from OCS-G-1972. The commitment under the approved contract was for 50 percent of the production. Amoco contends that it committed only 50 percent of its share of the production (*i.e.*, 25 percent of all production), leaving the remaining 50 percent of its share of production uncommitted. For 5 years 100 percent of Amoco's share of the production from the well was delivered to Columbia Gas. In 1977 the Federal Power Commission (FPC) approved the Columbia Gulf contract which, according to Amoco, was to cover the remaining 50 percent of its interest which it contends was not committed to Columbia Gas. According to Amoco, the Columbia Gulf agreement was for onshore delivery of gas to Florida Gas in partial satisfaction of the Florida Gas agreement. Amoco then delivered all of its production to Columbia Gulf and calculated the royalty

pursuant to the Florida Gas agreement. The stated purpose for doing so was to reduce that portion of the gas produced from the well and sold to Columbis Gas to 50 percent of Amoco's *total* production. However, even if we were to accept this argument, the value of production (for royalty purposes) is not subject to the accounting adjustment proposed by Amoco. Rather, royalties are calculated and paid monthly, and the effect of the sale to Columbia Gas during the initial 5-year period, for purposes of determining the basis for royalties, would be: (1) For 50 percent of the gas produced—the Columbia Gas agreement; (2) for the remaining gas—the value of equivalent gas as established by the Columbia Gas agreement. *See* 30 CFR 218.50.

[1] The question we must now consider is whether, during the 1977 through 1981 period, the price actually paid for the product or a higher price represents the value for royalty computation purposes. It is clear the Secretary is not limited to the actual value received, and we reaffirm the finding made in our initial decision: "[T]he valuation of the gas produced under lease OCS-G 1972 is governed by the August 1972 and March 1973 Survey value determination letters. Neither letter had been challenged or amended and they remained applicable for royalty determinations for gas produced during that time period." *Amoco Production Co., supra* at 127.

We again find and hold that MMS has regulatory authority to accept a FPC approved contract for royalty basis determination. If the FPC approved contract is designated as being applicable to production from a specific well, whether by the contract terms or by MMS, the FPC contract price will be binding on MMS, unless and until MMS rescinds or amends its acceptance of such valuation basis. Nothing in the original *Amoco* decision was intended to limit the discretionary decisionmaking

authority of the Secretary or his authorized agents, if that authority is properly exercised. However, a value determination letter cannot be construed in a manner which would result in the delegation to a lessee of the discretionary authority to set the value of gas sold.

The value determination letters provide that the value of production shall be the "FPC approved price, or a higher price, if received." Appellant urged this Board to accept the Florida Gas price, because the Florida Gas contract had received FPC approval and no higher price had been received. Appellant argues the Florida Gas price was binding because it was an FPC approved price, as set forth in the value determination letters. However, the MMS discretionary authority to allow calculation of the royalty pursuant to an FPC approved sales price does not extend as far as appellant would like it to be extended. To do so would be contrary to *both* the regulation as now in effect, and the regulation in effect prior to the 1979 amendment.[1] If the royalty determination were made on the basis of the Florida Gas contract, merely because the Florida Gas contract had FPC approval, it would result in a de facto delegation of the MMS responsibility for making a royalty determination (after considering *all* of the factors found in 30 CFR 250.64) and would be contrary to the regulation. The above quoted language in the value determination letters cannot be used as the basis for a finding by MMS or this Board that *any* FPC approved contract chosen by Amoco would, by reason of Amoco's election, become binding on MMS until such time as MMS would rescind Amoco's determination.

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[1] The only basis by which the supervisor (or this Board) could find the Florida Gas contract to be applicable would be pursuant to that language of the regulation in effect until 1979, which states: "*In the absence of good reason to the contrary,* * * *.* [sic] 30 CFR 250.64 (1977) (emphasis added).

With the above in mind, we make the following observations regarding the prior *Amoco* opinion. As noted above, 30 CFR 250.64 provides the criteria MMS is to apply when calculating royalty value. Between September 1977 and October 26, 1979, the applicable regulation, 30 CFR 250.64, stated:

> § 250.64 Value basis for computing royalties.
>
> The value of production, for the purpose of computing royalty, shall be the estimated reasonable value of the product as determined by the supervisor, due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field or area, to the price received by the lessee, to posted prices, and to other relevant matters. Under no circumstances shall the value of production of any of said substances for the purposes of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof or less than the value computed on such reasonable unit value as shall have been determined by the Secretary. In the absence of good reason to the contrary, value computed on the basis of the highest price paid or offered at the time of production in a fair and open market for the major portion of like quality products produced and sold from the field or area where the leased lands are situated will be considered to be a reasonable value.

On October 26, 1979, this regulation was amended, and the following language adopted:

> § 250.64 Value basis for computing royalties.

> The value of production shall never be less than the fair market value. The value used in the computation of royalty shall be determined by the Director. In establishing the value, the Director shall consider: (a) The highest price paid for a part or for a majority of like-quality products produced from the field or area; (b) the price received by the lessee; (c) posted prices; (d) regulated prices; and (e) other relevant matters. Under no circumstances shall the value of production be less than the gross proceeds accruing to the lessee from the disposition of the produced substances or less than the value computed on the reasonable unit value established by the Secretary.

30 CFR 250.64 (1980); 44 FR 61886 (Oct. 26, 1979).[2] The above language remained in effect for the balance of the period in question. As we found in *Amoco, supra* at 127, valuation of gas produced from lease OCS-G-1972 was governed by the value determination letters. We specifically find this to be the case for the 50 percent of Amoco's production committed to Columbis Gas. The Columbia Gas contract submitted by Amoco committed 50 percent of the production from OCS-G-1972 to Columbia Gas, and, for that portion of the production, the 1972 and 1973 letters were binding on MMS *and the producer,* unless and until rescinded or modified. *See* 30 CFR 250.47 (1982). While a copy of the Florida Gas contract had been submitted to MMS, there is ample evidence that there was no intent on the part of MMS to be bound by the terms of that contract with respect to the production from OCS-G-1972. This fact is clearly reflected by the conduct of the parties in the 5-year period preceding the audit period. Finally, we find,

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[2] This regulation was redesignated as 30 CFR 206.150 in 1983. 48 FR 35641 (Aug. 5, 1983).

for the 50 percent of the gas not committed to Columbia Gas, the royalty determination made by MMS was clearly with the discretionary authority of the Secretary as set forth in 30 CFR 250.64. It is based upon a regulated price (pursuant to the Columbia Gas contract) for the product of the well which has been accepted by the parties as being either the "estimated reasonable value" (pre-1979) or "fair market value" (post-1979).

The remaining two questions raised by the parties, as outlined above, point to a problem, which arises not from the Board's holding in the decision cited as *Amoco Production Co.*, 85 IBLA 121 (1985), but from dicta in that decision. Beginning with footnote 3 at page 128, and continuing with the text of the first paragraph on page 129, the Board's discussion of the effect which the amendment of 30 CFR 250.64 may have had upon the 1972 and 1973 value determination letters, and the effect of the regulatory amendment itself, were unnecessary to the decision of this appeal and have been criticized by both parties in their requests for reconsideration of the decision. Both parties have noted the possibility that these portions of the decision can be construed as being inconsistent with the Board's holding in this case. Upon reconsideration we recognize this discussion unnecessarily detracted from the holding by the Board. Accordingly, we hereby strike footnote 3 and the first paragraph on page 128 of the decision. The remainder of the Board's decision in *Amoco Production Co., supra*, is affirmed, as clarified by this decision. The Board specifically reaffirms the prior holding that the value of production for all of the gas from lease OCS-G-1972 during the 1977 through 1981 period involved was the price set in the Columbia Gas contract and approved by the August 1972 and March 1973 Survey letters, since no higher price was received.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision in *Amoco Production Co.*, 85 IBLA 121 (1985), is affirmed as modified by this decision.

/s/ R.W.Mullen
R. W. Mullen
Administrative Judge

I concur:

/s/ Franklin D. Arness
Administrative Judge

ADMINISTRATIVE JUDGE IRWIN CONCURRING IN THE RESULT:

Our holding holds and our dicta do not: that is all the parties ask us to clarify and all we need to say.

/s/ Will A. Irwin
Will A. Irwin
Administrative Judge

APPENDIX E

UNITED STATES DEPARTMENT OF THE INTERIOR

OFFICE OF HEARINGS AND APPEALS
INTERIOR BOARD OF LAND APPEALS
4015 WILSON BOULEVARD
ARLINGTON, VIRGINIA 22203

AMOCO PRODUCTION CO.

IBLA 84-789 Decided February 15, 1985

Appeal from decision of the Director, Minerals Management Service, affirming an order requiring payment of additional royalties on gas produced under Outer Continental Shelf oil and gas lease. MMS-82-0046-OCS.

Affirmed.

1. Oil and Gas Leases; Royalties—Outer Continental Shelf Lands Act: Oil and Gas Leases

   Where the lessee under an outer continental shelf oil and gas lease diverts gas produced under the lease from buyer A to buyer B in order to fulfill a warranty contract and computes royalty on the basis of the contract price to B, the Minerals Management Service may properly recompute the royalty based on the contract price to A where the price that would have been paid by buyer A represents the reasonable unit value of production under 30 CFR 250.64 (1982), *i.e.*, the highest price which could be received for the gas at the time of production, despite prior approval of use of the warranty contract price for calculation of royalties for gas produced under other leases.

APPEARANCES: George J. Domas, Esq., Deborah Bahn

Price, Esq., Bruce V. Schewe, Esq., New Orleans, Louisiana, for appellant; Charles R. Shockey, Esq., Office of the Solicitor, U. S. Department of the Interior, Washington, D.C., for the Minerals Management Service.

OPINION BY ADMINISTRATIVE JUDGE MULLEN

Amoco Production Company (Amoco) has appealed from a decision of the Director, Minerals Management Service (MMS), dated May 17, 1984, affirming an order issued by the Chief, Royalty Compliance Office, MMS, Tulsa, Oklahoma, dated September 20, 1982 (revised October 5, 1982), requiring payment of $1,435,852.97 in additional royalties for natural gas produced under lease OCS-G 1972, East Cameron Block 33, Offshore Louisiana, during the period from September 1977 to October 1981.

In his September 1982 order, the Chief, Royalty Compliance Office, concluded that appellant had undervalued natural gas produced between September 1977 and October 1981 by basing the royalty payments on the contract price set in a November 20, 1964, contract with Florida Gas Transmission Company (Florida Gas), which received the natural gas produced and shipped during the period in question, rather than the contract price set in a July 31, 1972, contract with Columbia Gas Transmission Corporation (Columbia Gas), which had previously received the natural gas. MMS noted that appellant had submitted the Columbia Gas contract to the Geological Survey (Survey) (MMS' predecessor in functions concerning offshore mineral lease management) on August 25, 1972, in accordance with 30 CFR 250.47 (1972) (redesignated 30 CFR 210.150 (1984)). This contract was submitted under cover of a letter which stated that, under the Columbia Gas contract "Amoco dedicates its share of gas produced from

the East Cameron Block 33 Field [OCS-G 1972 lease] to Columbia Gas Transmission Corporation." MMS further explained:

> Based upon Amoco's submission, a determination was made that the FPC [Federal Power Commission] rates approved for shipments from East Cameron Block 33 to Columbia Gas Transmission Corporation represented the value basis for computing royalties in accordance with the requirements of 30 CFR 250.64 [(1982)], and [Survey] issued Amoco a letter dated August 31, 1972, which stated, "We have received your Gas Purchase and Sales Agreement dated July 31, 1972, with Columbia Gas Transmission Corporation, covering the sale of your share of gas produced from lease OCS-G 1972, East Cameron Block 33. Payment on the gas for royalty purposes shall be based on the field delivery volume times the FPC approved price, or a higher price, if received."
>
> Royalty payments submitted to MMS through August 1977 were based upon the FPC-approved rates for shipments from East Cameron Block 33 to Columbia Gas Transmission Corporation. In September 1977, Amoco began to ship a majority of its share of the gas from East Cameron Block 33 to Florida Gas Transmission Company. It is our understanding that the shipments were made to Florida Gas Transmission Company under a transportation agreement approved by FERC [(Federal Energy Regulatory Commission), the successor to the FPC] in September 1977 between Amoco and Columbia Gulf Transmission Corporation where gas is delivered from East Cameron Block 33 to Florida Gas Transmission Company at a point in St.

> Landry Parish, Louisiana. We found no evidence that Amoco submitted to MMS the above transportation agreement or the Florida Gas Transmission Company contract as required by 30 CFR 250.47 [(1982)] for the disposal of lease products or to establish the value basis for computing royalties under the requirements of 30 CFR 250.64 [(1982)]. Beginning at this time and continuing through October 1981, the royalty payments to MMS were based upon the Florida Gas Transmission contract price of $.2125 Mcf.
>
> A meeting with Amoco personnel was held on August 13, 1982, in the Tulsa MMS office to discuss the issue and ascertain Amoco's position. At that time, Amoco did not refute the fact that they had never requested nor received approval from MMS to sell gas production from East Cameron Block 33 to Florida Gas Transmission Company. The only approval for sales of production from East Cameron Block 33 requested and received by Amoco was the value determination letter from [Survey] dated August 31, 1972, covering sales to Columbia Gas Transmission Corporation.

MMS concluded that: "Since Amoco failed to adhere to the requirements of 30 CFR 250.47 [(1982)] and 30 CFR 250.64 [(1982)], MMS recomputed its royalties based upon the August 31, 1972, value determination letter and Amoco's fifty percent (50%) allocated share of the non-unit production and Amoco's sales from the unit production." MMS required appellant to submit the additional royalties "not later than October 15, 1982."

On October 13, 1982, appellant filed a notice of appeal from the September 1982 order to the Director, MMS. In its brief on appeal, appellant explained that it had submitted a copy of the November 1964 Florida Gas contract

to Survey on June 29, 1966, under a cover letter that stated that the contract "does not provide for the present commitment or dedication to Florida [Gas] of specific leases or fields." Appellant stated that the Florida Gas contract did not initially cover sales of gas produced under lease OCS-G 1972 and that no such gas was being produced at that time. Appellant also stated that it had submitted a copy of an order by the FPC dated September 15, 1965 (Docket No. CI 65-584), granting a certificate of public convenience and necessity with respect to the November 1964 Florida Gas contract, essentially approving the Florida Gas contract, including the stated contract price. In addition, the order required the sellers to give notice to FPC identifying each field and each producer delivering gas to Florida Gas at the time of commencement of deliveries of gas from any particular field.[1] Appellant also stated that the July 1982 Columbia Gas contract specifically provided that only 50 percent of the gas produced from lease OCS-G 1972 was committed to Columbia Gas.[2] Appellant also submitted an affidavit by Brian J. Heisler, dated October 8, 1982. In his affidavit Heisler explained that, pursuant to a contract with Columbia Gulf Transmission Company (Columbia Gulf), the remaining 50 percent was to be delivered offshore to Columbia Gulf, an affiliate of Columbia Gas for delivery

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[1] The record indicates that appellant notified FERC on Jan. 10, 1979, that it was delivering gas to Florida Gas from the East Cameron Block 33 Field, Louisiana, pursuant to the November 1964 Florida Gas contract.

[2] As further proof that Survey was aware that the Columbia Gas contract had committed only 50 percent of the gas produced to Columbia Gas, appellant submitted a copy of a Mar. 9, 1973, letter from the Acting Oil and Gas Supervisor, Gulf of Mexico Area, Survey, which states: "Amoco owns 50% of lease OCS-G 1972, East Cameron Block 33, and Mobil has the remaining 50%. Amoco has committed 50% of its share of the gas from this lease to Columbia Gas, with the remaining 50% of its share being uncommitted at this time."

onshore "in partial satisfaction of Amoco's prior contractual obligations to Florida Gas Transmission Company and Florida Power and Light Company." Heisler explained that until 1977, 100 percent of the gas produced under lease OCS-G 1972 was sold to Columbia Gas because of delays in FPC approval of the Columbia Gulf contract. He further explained that with FPC approval in 1977, in an effort to reduce total gas produced from lease OCS-G 1972 and sold to Columbia Gas to the 50 percent set in the Columbia Gas contract and satisfy appellant's prior obligations to Florida Gas, appellant delivered all of the gas produced to Florida Gas. Finally, appellant stated that in forwarding the Columbia Gas contract to Survey it had "inadvertently neglected to inform the [Survey] that the portion of the gas that was clearly not committed to Columbia under this contract would be sold to FGT pursuant to the FGT contract."

Appellant argues that it had complied with 30 CFR 250.47 (1982) which required it to file with the Director, MMS, a copy of all contracts for the disposal of leased products. Appellant states that it had submitted copies of the Columbia Gas and Florida Gas contracts, but was not required to submit a copy of the Columbia Gulf contract because the Columbia Gulf contract did not deal with the valuation of gas for royalty computation purposes. Appellant also argues that it computed and paid royalties between September 1977 and October 1981 consistent with the August 1972 Survey value determination letter, which required payment at the Florida Gas approved price, because the Florida Gas contract price had been approved by FPC. Appellant noted that "on or about February 2, 1977," Survey in part approved the Florida Gas contract for computation of royalties for gas produced from leases other than OSC-G [sic] 1972 (Amoco Brief at 9). Finally, appellant contended that MMS and Survey has consistently accepted royalty payments for gas produced from various

leases, including lease OCS-G 1972, through October 1981 based on the Florida Gas contract price and cannot retroactively change the method of royalty computation, citing *Superior Oil Co.*, 12 IBLA 212 (1973) (Statement of Reasons at 12; Letter dated December 16, 1982, Domas to MMS).

In his May 1984 decision affirming the September 1982 order, the Director, MMS, concluded that the "FPC approved price" referred to in the August 1972 Survey value determination letter was the Columbia Gas Contract price, *i.e.*, "the only price established by FPC for production from [lease OCS-G 1972]" (Decision at 3). MMS noted that a March 9, 1973, Survey letter to appellant indicates that the Columbia Gas contract price would apply to all gas produced under lease OCS-G 1972. MMS also stated that it was justified in demanding additional royalties on the basis of the earlier value determination letter, when it discovered that appellant was submitting royalties on a "different basis," despite its prior acceptance of such royalties, citing *Supron Energy Corp.*, 46 IBLA 181 (1980), *appeal filed sub nom. Conoco v. Andrus*, Civ. No. 80-0261 M (D.N.M. Apr. 17, 1980) (Decision at 4). Finally, MMS stated that it was entitled to apply the Columbia Gas contract price regardless of the fact that appellant had submitted copies of the Florida Gas and Columbia Gas contracts, the "voluntary diversion" of gas produced from lease OCS-G 1972 by appellant, or the royalty values for gas produced under "other leases." *Id.* at 4.

In its statement of reasons for appeal, appellant contends that, when the August 1972 and March 1973 value determination letters were issued by Survey, Survey was aware that appellant was committing only 50 percent of its share of the gas produced from lease OCS-G 1972 to Columbia Gas. Appellant contends that if the oil and gas super-

visor had intended the term "FPC-approved price" to mean only the Columbia Gas contract price, he would have so stated. Appellant alleges that it has paid all royalties based on the "FPC-approved price." Appellant also states that it has not voluntarily diverted gas to Florida Gas to avoid paying royalties at the Columbia Gas contract price, as MMS intimates, but has merely complied with the Columbia Gas contract and prior Florida Gas contract commitments. Finally, appellant contends that MMS' valuation of gas produced under lease OCS-G 1972 and sold to Florida Gas at a price in excess of the FPC-approved price to Florida Gas, is inconsistent with the February 1977 Survey approval of the Florida Gas contract price for sales of gas from other leases and the findings in *Amoco Production Co.*, IBLA 82-714, which culminated in Departmental recognition that the "FPC-approved contract price for gas sold to [Florida Gas] is the proper basis for the payment of royalties." Appellant concludes that this inconsistent treatment is arbitrary and capricious, citing *Keen Transport, Inc. v. United States*, 446 F. Supp. 5 (N.D. Ohio 1976)(Statement of Reasons at 11, 12). Appellant states that, for these reasons, MMS is not entitled to additional royalties.

In an answer to appellant's statement of reasons, MMS contends that the valuation of all gas produced under lease OCS-G 1972 for royalty computation purposes is governed by the August 1972 and March 1973 Survey value determination letters. MMS interprets the reference to "FPC-approved price" to mean the Columbia Gas contract price. MMS notes that appellant has requested a value determination for the total of its share of gas produced under the lease, and not just that portion committed to Columbia Gas. MMS argues that appellant cannot subsequently sell to Florida Gas at a reduced price, thereby unilaterally altering the "Secretary's right to receive royalties under the 1973 settlement," noting that appellant

has neither contested nor sought to amend the 1973 settlement (Answer at 8,9). MMS notes that the Columbia Gas contract price, the highest price received for similar gas, is considered by MMS to be the appropriate royalty valuation price consistent with 30 CFR 250.64 (1982) (redesignated 30 CFR 206.150 (1984)), and the Board's decision in *Amoco Production Co.*, 78 IBLA 93 (1983), *appeal filed, Amoco Production Co. v. Clark*, Civ. No. CV 84-0916 (W.D. La. Apr. 6, 1984).

MMS stresses that the August 1972 and March 1973 Survey value determination letters constituted a settlement of appellant's royalty obligation with respect to gas produced under OCS-G 1972 and, in fact, was applied to all gas produced and sold "for almost five years." MMS contends that appellant was required to propose a "new settlement using the [Florida Gas] contract price" when it began sales to Florida Gas and that, having failed to do so, appellant remained bound by the 1972 and 1973 settlement (Answer at 12, 13).

MMS argues that even if the settlement between appellant and MMS and reflected by the 1972 and 1973 letters applied only to the 50 percent of the gas actually committed to Columbia Gas, the Columbia Gas contract price was the highest price received for similar gas under 30 CFR 250.64 (1982), and thus was applicable to the remaining 50 percent of the gas sold to Florida Gas (or anyone else).

MMS argues that the fact that it accepted royalties based on the February 1977 Survey decision with respect to other leases does not alter the validity of the 1972 and 1973 settlement with respect to lease OCS-G 1972, because the Secretary has the discretionary authority "to establish an appropriate royalty valuation for each lease" (Answer at 17). MMS also argues that its actions in response to a remand in *Amoco Production Co.*, IBLA 82-714, did not con-

stitute a recognition of the Florida Gas contract price as the proper basis for determining the royalties due under lease OCS-G 1972. MMS contends that since September 1977 appellant has been able, but simply unwilling, to sell gas produced under lease OCS-G 1972 at the Columbia Gas price and has the ability to meet the Florida Gas commitment by delivery of gas from other sources, concluding that the Government should not lose royalty revenues because of appellant's unilateral decision to deliver gas produced from lease OCS-G 1972 to Florida Gas.

[1] Prior to the 1978 amendment of section 8(b) of the Outer Continental Shelf Lands Act (OCSLA), 43 U.S.C. § 1337(b) (1976), this section required the payment of royalty of "not less than 12-½ per centum, in the amount or value of the production saved, removed, or sold from the lease." While OCSLA does not specify the method for valuing production, we recognized in *Amoco Production Co., supra* at 96, that the Secretary has "considerable discretion for determining what is the 'value' of production." This discretion has been exercised in part by the promulgation of 30 CFR 250.64 (1982), which governs the valuation of production for royalty computation purposes.

In 1977 when appellant began its sales of gas to Florida Gas, 30 CFR 250.64 (1977) provided that the value of production shall be determined with "due consideration being given to the highest price paid for a part or for a majority of production of like qualtiy in the same field or area, to the price received by the lessee, to posted prices, and to other relevant matters." In addition, the regulation provided:

> Under no circumstances shall the value of production of any of said substances for the purposes of computing royalty be deemed to be less than the gross proceeds accuring to the lessee from the

> sale thereof or less than the value computed on such reasonable unit value as shall have been determined by the Secretary.

Id. The regulation was amended effective December 13, 1979, but the above-quoted portion of the regulation was not substantially changed. *See* 44 FR 61886, 61903 (Oct. 26, 1979); 30 CFR 206.150 (1984).

MMS contends that valuation of gas produced under lease OCS-G 1972 is primarily governed by the August 1972 and March 1973 Survey value determination letters. In appellant's letter, dated August 23, 1972, transmitting the Columbia Gas contract to Survey, appellant stated that under the contract "Amoco dedicates its share of gas produced from the East Cameron Block 33 Field to Columbia Gas Transmission Corporation." The letter does not indicate that appellant was dedicating 50 percent of "its share of gas produced," rather than 100 percent. Thus, when Survey, in its August 1972 letter, determined that payment on "the gas" for royalty purposes should be based on the "FPC-approved price, or a higher price, if received," it appears that Survey intended the determination to apply to appellant's share of gas produced under lease OCS-G 1972. Appellant had not informed Survey that only 50 percent of its share of gas produced was being committed to Columbia Gas.

Appellant argues that any misconception was subsequently clarified by a February 20, 1973, letter to the Oil and Gas Supervisor, Gulf Coast Region, Survey, which specifically stated that 50 percent of appellant's share of the gas produced was "uncommitted." In this letter appellant also requested that MMS approve appellant's proposal

> to compute royalty in the following manner on gas produced from the above-mentioned lease and which is processed in the South Pecan Lake Plant. *** The total value of the gas and products shall not be less than the field-metered volume times the FPC-approved price, or the higher price if received.

As can be seen, appellant's letter does not limit the approval of the valuation to that gas to be sold to Columbia Gas. The March 1973 Survey value determination letter, which approved appellant's valuation method, recognizes that 50 percent of appellant's share of gas produced under lease OCS-G 1972 is "uncommitted." While this supports appellant's allegation, the determination letter approves the value "for Amoco's share of the gas from the above lease," rather than 50 percent of Amoco's share. The letter does not state that the valuation method would apply only to that gas to be sold to Columbia Gas. Thus, we conclude that Survey's reiteration in the March 1973 letter that the value of gas produced shall be the "FPC-approved price or a higher price if received" applies to all gas produced under lease OCS-G 1972. We, therefore, agree with MMS that the valuation of gas produced under lease OCS-G 1972 is governed by the August 1972 and March 1973 Survey value determination letters. Neither letter had been challenged or amended and they remained applicable for royalty determinations for gas produced during that time period.

However, we do not agree with MMS that the term "FPC-approved price" is equivalent to the Columbia Gas contract price. Appellant was selling 100 percent to its share of the gas produced under lease OCS-G 1972 to Columbia Gas when the March 1973 Survey value determination letter was issued. However, the letter also indicates

that Survey was aware that only 50 percent of appellant's share of gas produced was committed to Columbia Gas. This being the case, appellant could choose to sell the uncommitted portion of its share of production to other parties. The letter refers to the "FPC-approved price," rather than the "FPC-approved price for sales to Columbia Gas." We conclude that the lack of language specifically stating that the Columbia Gas price would be controlling reflects Survey's intent to value production based on an FPC-approved price or price received when appellant sold gas at a price higher than the FPC-approved price. This is consistent with 30 CFR 250.64 (1982) which requires that production be valued at not less than the gross proceeds received from the sale of lease products.

MMS argues in the alternative that, even if the August 1972 and March 1973 Survey value determination letters did not specifically incorporate the Columbia Gas contract price for calculation of sales to Florida Gas, the Columbia Gas contract price represents a "reasonable unit value" under 30 CFR 250.64 (1982). In *Amoco Production Co., supra* at 100, we recognized that MMS has the authority to superimpose a value determination "based on actual market conditions on any sales price which falls below the standard of reasonableness," such that the reasonable unit value of production is not less than the highest price received for similar gas. In that case, Amoco was not prevented from selling gas at the higher price because gas produced from lease OCS-G 2866 and sold pursuant to a warranty contract had not been committed to the warranty contract. Thus, Amoco could have chosen to sell that production pursuant to any other contract. In the present case, MMS argues that the Columbia Gas contract price should be superimposed on the Florida Gas contract price because the Florida Gas contract was a warranty contract which therefore did not require the gas delivered under the con-

tract to come from any specific well, and because the Columbia Gas contract price represents the "reasonable unit value" or the highest price which could be received for sales of gas produced under OCS-G 1972. There can be no question that the gas was similar.

Initially, it appears that MMS ignored the fact that valuation of production is governed by the Survey value determination letters, which are an implementation of Survey's authority under 30 CFR 250.64 (1982). These letters provide that the value of production shall be the "FPC-approved price, or a higher price *if received.*" Thus, the terms of these letters would appear to provide for valuation of production at an FPC-approved price (the Florida Gas contract price), or at a higher price where a higher price (the Columbia Gas contract price) had been paid. The latter limitation is a reflection of the language in 30 CFR 250.64 (1982) that the value of production should be not less than the gross proceeds accuring to the lessee from the actual sale of lease products. However, the Survey value determination letters cannot be said to conclude that the FPC-approved price or higher price received are, per se, the "reasonable unit value" for gas produced and sold under lease OCS-G 1972 as is required by 30 CFR 250.64 (1982). In *Amoco Production Co., supra* at 100, the Board recognized the fact that the reasonable unit value "may not be less than the highest price received for similar gas." Indeed, 30 CFR 250.64 (1977) provided that:

> In the absence of good reason to the contrary, value computed on the basis of *the highest price paid or offered at the time of production* in a fair and open market for the major portion of like-quality products produced and sold from the field or area where the leased lands are situated *will be considered to be a reasonable value.* [Emphasis added.]

See Getty Oil Co., 51 IBLA 47, 51 (1980). We conclude that the Florida Gas contract price was consistent with the Survey value determination letters, but that this price did not represent the highest price which could be received for similar gas produced under lease OCS-G 1972 pursuant to 30 CFR 250.64 (1982). The "reasonable unit value" was represented by the Columbia Gas contract price. The Columbia Gas contract remained in effect and gas produced from lease OCS-G 1972 could have been sold pursuant to the Columbia Gas contract. 30 CFR 250.64 (1982) is controlling. While there is no question that between September 1977 and October 1981 appellant had the right to sell gas produced under lease OCS-G 1972 to Florida Gas, the Department is entitled to collect royalties on the basis of the highest price received for similar gas. In this case, that price is the Columbia Gas contract price.[3]

Appellant also argues that, when MMS refused to use the Florida Gas contract price when setting a value on gas produced under lease OCS-G 1972 and sold to Florida

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[3]On appeal to the Board, appellant has apparently dropped its argument that the September 1982 MMS order constituted an improper retroactive change of the method of royalty computation. The Director, MMS, responded contending that MMS was merely applying August 1972 and March 1973 Survey value determination letters when recomputing appellant's royalties. As noted above, the letters had been superseded by 30 CFR 250.64 (1982), which required recomputation of royalties on the basis of the highest price which could be received for sales of similar gas. As we observed in *Supron Energy Corp., supra* at 189 n.6: "where the Department directs lesses (even explicitly) to compute royalty in a manner which is beyond its authority to allow, it is *not* estopped by its acceptance of the erroneous payments from correcting its error. *Atlantic Richfield Co. v. Hickel*, 432 F.2d 587, 591 (10th Cir. 1979)." (Emphasis in original.) *See also Gulf Corp.*, 21 IBLA 1 (1975); *Superior Oil Co., supra* at 226 n.10. In the present case, the Survey value determination letters were contrary to 30 CFR 250.64 (1982). The value of production must be at least equal to the reasonable unit value. MMS was not estopped from recomputing royalties consistent with the regulation by acceptance of royalties computed pursuant to the determination letters.

Gas, it acted in an inconsistent manner. Appellant refers first to a February 1977 Survey letter which stated that the value for gas produced from certain other leases and sold to Florida Gas was the FPC-approved Florida Gas contract price. MMS argues this is permissible because the 1977 value determination letter is applicable only to the sale of gas produced from the other leases. However, MMS overlooks the fact that the gas sold to Florida Gas was also produced by Amoco and offers no explanation for the different treatment. Nevertheless, as noted above, the MMS' evaluation in this case is governed by 30 CFR 250.64 (1982), not the August 1972, the March 1973, or even the 1977 Survey value determination letter. Neither MMS nor the Board may ignore a duly promulgated regulation of the Department. *Sam P. Jones,* 71 IBLA 42 (1983).

Appellant also argues that, as a result of the remand in *Amoco Production Co.*, IBLA 82-714, the Department has recognized the Florida Gas contract price as the proper basis for royalty computation for gas sold to Florida Gas. In response, MMS states that the remand and subsequent vacation of the MMS order giving rise to this appeal merely reflected "a decision to review policy" after the remand of the other *Amoco* case and that the May 1984 decision which is the subject of this appeal herein resulted, in part, from this policy review. Appellant has presented no evidence that MMS has made a formal determination that the Florida Gas contract price was the proper basis for computing royalties due to the United States for gas produced under lease OCS-G 1972. Accordingly, we conclude that MMS has not acted in a manner which is inconsistent with *Amoco Production Co., supra.*

Where a party challenges a determination as to the value of gas or other hydrocarbons produced from a lease with the United States, the party must establish that the

methodology used is, in fact, erroneous. *Supron Energy Corp.*, 55 IBLA 318, 322 (1981), *appeal filed sub nom. Atlantic Richfield Co. v. Watt*, Civ. No. 81-0615 (D.N.M. filed July 29, 1981). Appellant, however, has failed to demonstrate error in the May 1984 MMS decision upholding the September 1982 royalty recomputation.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision appealed from is affirmed.

/s/ R. W. Mullen
R. W. MULLEN
Administrative Judge

We Concur:

/s/ Franklin D. Arness
Franklin D. Arness
Administrative Judge

/s/ Will A. Irwin
Will A. Irwin
Administrative Judge

(2)

Supreme Court, U.S.
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No. 89-454

In the Supreme Court of the United States

OCTOBER TERM, 1989

AMOCO PRODUCTION COMPANY, PETITIONER

v.

MANUEL LUJAN, JR., SECRETARY,
DEPARTMENT OF THE INTERIOR, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENTS IN OPPOSITION

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QUESTION PRESENTED

Whether the Department of the Interior acted arbitrarily or contrary to law when it determined that petitioner, a lessee to government-owned mineral rights, had underpaid royalties on gas produced under its lease from 1977 through 1981.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A1-A22) is reported at 877 F.2d 1243. The memorandum ruling of the district court (Pet. App. A23-A34) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on July 24, 1989. The petition for a writ of certiorari was filed on September 18, 1989. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. The Secretary of the Interior is authorized by the Outer Continental Shelf Lands Act of 1953, 43 U.S.C. 1331 *et seq.*, to grant leases for the recovery of minerals, including oil and gas, from the seabed of the Outer Continental Shelf. 43 U.S.C. 1337 (1982 & Supp. V 1987). The

Act requires the Secretary "to assure the receipt of fair market value for the lands leased and the rights conveyed," 43 U.S.C. 1344(a)(4), and further requires the lessee to pay the government a royalty that relates to "the amount or value of the production saved, removed, or sold." 43 U.S.C. 1337(a)(1)(A). The Minerals Management Service (MMS) administers this program for the Department of the Interior.

The Secretary has issued regulations establishing the standards for determining the "value of production" for royalty purposes. In 1954, the Secretary promulgated a regulation (30 C.F.R. 250.64 (1955)) granting the United States Geological Survey (USGS)[1] broad discretion to determine the "value of production" for royalty purposes:

> The value of production, for the purposes of computing royalty, shall be the estimated reasonable value of the product as determined by the supervisor, due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field or area, to the price received by the lessee, to posted prices, and to other relevant matters. * * *

30 C.F.R. 250.64.

The Secretary amended the regulation in 1979 (30 C.F.R. 250.64 (1980)) to state explicitly: (1) that "[t]he value of production shall never be less than the fair market value," as required by the statute; (2) that "the computation of royalty shall be determined by the Director" of MMS; and (3) that the Director "shall consider" certain factors "[i]n establishing value" (*ibid.*).[2] At all times, the

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[1] USGS administered the lease program until that function was transferred to MMS. Pet. App. A6.

[2] The amended regulation stated in full:

> The value of production shall never be less than the fair market value. The value used in the computation of royalty shall be

regulations have set the minimum royalty value as the "gross proceeds" received by the lessee – *i.e.*, the total consideration. The regulations, however, allow the Director of MMS to determine that the "value of production" for a particular lease is higher than the lessee's gross proceeds. The Director may set a higher value by considering, among other things, the prices paid for like-quality products from the same field or area.

Lessees must "file with the Director, within 30 days after their effective date, a copy of all contracts * * * for the disposal of lease products." 30 C.F.R. 210.150 (1983). Lessees pay royalties on a monthly basis, 30 C.F.R. 218.50, but those payments are subject to a later audit by MMS's Royalty Compliance Office. 30 C.F.R. 217.200 (1983).

2. Petitioner owns a 50% share of the gas produced under a lease entered into with the United States in 1970 and called Lease OCS-G 1972 (Lease 1972). Pet. App. A6, A25-A26. In August 1972, petitioner filed with USGS copies of a gas-purchase contract between petitioner and Columbia Gas Transmission Corporation. *Id.* at A6-A7. Petitioner's accompanying letter explained that the agreement covered sales from Lease 1972, and stated that peti-

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determined by the Director. In establishing the value, the Director shall consider: (a) The highest price paid for a part or for a majority of like-quality products produced from the field or area; (b) the price received by the lessee; (c) posted prices; (d) regulated prices; and (e) other relevant matters. Under no circumstances shall the value of production be less than the gross proceeds accruing to the lessee from the disposition of the produced substances or less than the value computed on the reasonable unit value established by the Secretary.

30 C.F.R. 250.64 (1980). The regulation was redesignated in 1983 as 30 C.F.R. 206.150, and has since been modified in ways unrelated to this case.

tioner "dedicate[d]"[3] its share of gas produced under the lease to Columbia Gas. Admin. Rec. tab 37, Exh. C.

The USGS Supervisor then sent petitioner a letter (Pet. App. A19) acknowledging receipt of petitioner's contract with Columbia Gas and stipulating that "[p]ayment on the gas for royalty purposes shall be based on the field delivery volume times the [Federal Power Commission]-approved price, or a higher price, if received."[4] In February 1973, petitioner again wrote the USGS Supervisor: (1) to explain that the company had committed half of its 50% share to Columbia Gas but that the remaining gas was uncommitted, and (2) to seek the Supervisor's approval that royalties be not less than the volume of gas produced multiplied by the FPC-approved price, or a higher price if received. Admin. Rec. tab 35, Exh. L. The Acting Supervisor approved that method of valuation. Pet. App. A20-A22.

Until 1977, petitioner sold its entire share of Lease 1972 gas to Columbia Gas. Pet. App. A7. Petitioner paid

[3] "Dedicates" is a term of art in oil and gas purchase agreements, and is used in contrast to the term "warrants." Sales are most commonly made pursuant to a "dedication" or "commitment" contract like that between petitioner and Columbia Gas, in which the producer/seller identifies a particular source – here, Lease 1972 – that will be used to fulfill the contract for its full term. That source is then said to be dedicated or committed to that contract. A warranty contract, in contrast, is one in which the producer/seller agrees to provide a certain volume of product to the buyer over the life of the contract, *i.e.*, warrants that such volume will be provided, but does not specify the source or sources of the product to be provided. Accordingly, the producer/seller is free to fulfill a warranty contract from whatever source or combination of sources it chooses.

[4] Section 7 of the Natural Gas Act, 15 U.S.C. 717f, required that the Federal Energy Regulatory Commission (formerly the Federal Power Commission (FPC)) approve such gas sale contracts and prices, through issuance of a certificate of public convenience and necessity. 15 U.S.C. 717f(c).

royalties based on the Columbia Gas contract price (*ibid.*), and those royalty payments are not at issue here. From September 1977 to October 1981, however, petitioner sold its entire share of Lease 1972 gas to Florida Gas Transmission Company. *Id.* at A8, A27. Petitioner sold that gas under a warranty contract with Florida Gas that had been executed in 1964. For this period, petitioner made royalty payments on the basis of the Florida Gas contract price, which was substantially lower than the Columbia Gas contract price. *Id.* at A8. The Department was not notified of petitioner's decision to sell Lease 1972 gas under the Florida Gas contract. *Id.* at A16.[5]

The MMS Royalty Compliance Office audited petitioner's royalty payments for the years 1977 to 1981 and concluded that petitioner should have paid royalties based on the Columbia Gas contract price, not the Florida Gas contract price. Pet. App. A8. MMS gave two reasons for its decision: (1) the government's initial royalty valuation for Lease 1972 was made in connection with the Columbia Gas contract, and (2) petitioner had never sought any royalty valuation in connection with sales of Lease 1972 gas to Florida Gas. *Id.* at A47-A48. On appeal, the Director of MMS affirmed the Compliance Office's decision. *Id.* at A51.

Petitioner appealed the Director's decision to the Interior Board of Land Appeals. The Board affirmed the

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[5] Although a copy of the Florida Gas contract had been sent to USGS in 1966 (Pet. 6), that submission did not specify Lease 1972 as a source for gas under that contract because that letter predated Lease 1972 by four years. By letter of January 14, 1977, petitioner requested a royalty payment procedure for production from three other leases identified as providing gas for the Florida Gas contract. See Pet. 8; Admin. Rec. tab 37, Exh. E. However, no such letter was sent to MMS that identified Lease 1972 as an intended source for the Florida Gas "warranty" contract.

Director's determination that petitioner had underpaid its royalty obligation. Pet. App. A36-A61. In its opinion on reconsideration, the Board interpreted the applicable regulation, 30 C.F.R. 250.64 (1980), as vesting in MMS alone the authority to find "the value of production" from a specific lease. Pet. App. A40. The Board stated that such authority cannot be granted to the lessee. *Ibid.* The Board therefore reasoned that the royalty-valuation letters in this case bound the parties only insofar as they reflected a proper exercise of regulatory authority; thus they could not be construed in a way that would result in a delegation to petitioner of the authority to set the value of gas produced under Lease 1972. *Ibid.*

The Board accordingly rejected petitioner's proffered construction of the royalty-valuation letters that would have given petitioner the power to select the Florida Gas contract price as the "value of production" for the years 1977 through 1981. Pet. App. A40. And the Board concluded that the Director's selection of the Columbia Gas contract price for the years in question was a permissible exercise of the Director's discretion. *Id.* at A42-A43.

3. Petitioner then brought this suit challenging the Board's decision. The district court, performing the limited review authorized by the Administrative Procedure Act, 5 U.S.C. 706, reviewed the record and concluded that the Board's decision had "a rational basis" and was not a "clear error." Pet. App. A33. Thus the court granted the government's motion for summary judgment. *Id.* at A35.

4. The court of appeals affirmed. Pet. App. A1-A19. It held that "the Board acted within its authority by concluding that federal regulations prohibited the federal official charged with responsibility for valuing gas from delegating the authority to do so, and by further concluding that the construction of the [valuation] letters contended for by [petitioner] would involve such a delegation." Pet. App. A2. The court therefore held that

the Director of MMS retained the authority to determine the value of the disputed gas production, and that the valuation itself "was a reasonable exercise of his discretion." *Ibid.*

ARGUMENT

The decision of the court of appeals is correct, and it does not conflict with the decisions of any other court. Thus no further review is warranted.

1. Petitioner's main contention (Pet. 13-21) is that the court of appeals erred by condoning "the Department's retroactive application of a new interpretation of the pertinent statutes and regulations." Pet. 17. But this is not a case of retroactive application of the Department's regulations. The Department had never before faced the question presented by this case; and it most definitely had never before permitted the result that petitioner wished to obtain. This is the first time that the Department has been required to construe its own regulations to determine whether MMS must decide the value of production under a lease, or whether the Department may (as petitioner contends) delegate that function to the lessee. The Department determined that, under 30 C.F.R. 250.64 (1980), MMS must make that finding. Hence, the only question presented is whether the Department's interpretation of its own regulations should be set aside.

The court of appeals, of course, properly deferred to the Department's view of its own regulation. It is well settled that "[i]n construing administrative regulations, 'the ultimate criterion is the administrative interpretation, which becomes of controlling weight unless it is plainly erroneous * * *.' " *United States* v. *Larionoff*, 431 U.S. 864, 872 (1977). See also *INS* v. *Stanisic*, 395 U.S. 62 (1969).

Here, the court of appeals correctly held (Pet. App. A16) that the Board's interpretation of the Department's regulation was reasonable.

The Outer Continental Shelf Lands Act requires that lessees pay royalties based on "the amount or value of the production saved, removed, or sold." 43 U.S.C. 1337(a)(1)(A). And the Department's applicable regulation under the Act, 30 C.F.R. 250.64 (1980), states that such "value of production" for royalty valuation purposes "*shall* be determined" by the Director of MMS, on the basis of a specified list of factors, including the highest price paid for like-quality gas from the same field (emphasis added). Accordingly, the Board reasonably concluded that, under the Department's regulation, only the Director of MMS has the authority to determine the "value of production" under a lease; that task cannot be delegated to the lessee when it decides how to dispose of its gas.[6]

At bottom, petitioner's claim appears to be based on estoppel principles—*i.e.*, that the government's valuation letters led petitioner to believe that it could pay royalties under the 1972 Lease on the basis of *any* FPC-approved price. At the time the Department issued its valuation letters, however, petitioner had not submitted the Florida Gas contract to the government. As the court of appeals recognized (Pet. App. A16-A17), therefore, this is not a case where the Department made an informed and responsive valuation decision and, later, tried to change that decision.

2. Contrary to petitioner's suggestion (Pet. 18-19), the Department did not act arbitrarily or abuse its discretion in selecting the Columbia Gas contract price as the value

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[6] Under petitioner's construction of the valuation letters, petitioner could control the determination of the "value of production" by choosing to sell Lease 1972 gas under any of its many FPC-approved warranty contracts.

of production under Lease 1972. The Florida Gas contract was never designated by petitioner as being applicable to Lease 1972. The only contract so designated was petitioner's contract with Columbia Gas. Petitioner was not contractually bound to sell Lease 1972 gas at the Florida Gas contract price, nor was petitioner bound to sell the gas to Florida Gas at all.

For reasons of its own, petitioner chose to use Lease 1972 gas to fulfill an old contractual obligation to Florida Gas. But unlike the Florida Gas contract, the Columbia Gas contract specifically pertained to gas produced under Lease 1972 and represented market conditions related to Lease 1972's operations. See Pet. App. A59. Thus, MMS did not abuse its discretion in selecting the Columbia Gas contract price as representing the value of production under Lease 1972 for years 1977 through 1981.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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